United States Court of Appeals

for the

District of Columbia Circuit

TRANSCRIPT OF RECORD

FOR MR. JUSTICE VAN ORSDEL

TRANSCRIPT OF RECORD

Court of Appeals of the District of Columbia

OCTOBER TERM, 1932

No. 5858 309

ALWORTH-WASHBURN COMPANY, APPELLANT,

Guy T. Helvering, vs.

~~DAVID BURNET,~~ COMMISSIONER OF INTERNAL REVENUE.

APPEAL FROM THE BOARD OF TAX APPEALS.

FILED NOVEMBER 26, 1932.

PRINTED JANUARY 12, 1933.

Oct. 10/33

Court of Appeals of the District of Columbia

OCTOBER TERM, 1932

No. 5858

ALWORTH-WASHBURN COMPANY, APPELLANT,

vs.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE.

APPEAL FROM THE BOARD OF TAX APPEALS.

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JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., DECEMBER 6, 1932.

Court of Appeals of the District of Columbia

No. 5858.

ALWORTH-WASHBURN COMPANY, Appellant,

vs.

DAVID BURNET, Commissioner of Internal Revenue.

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1 Docket No. 45651.

ALWORTH-WASHBURN CO.

vs.

COMMISSIONER OF INT. REV.

For Taxpayer: Frank W. Wilson, C. P. A.; Paul E. Shorb, Esq.; A. C. Washburn, Esq.

For Commissioner: A. H. Fast, Esq.

Docket Entries.

1929.

Sept. 9. Petition received and filed. Taxpayer notified. Fee paid.

" 10. Copy of petition served on General Counsel.

Oct. 24. Answer filed by G. C.

Nov. 1. Copy of answer served on taxpayer—General Calendar.

1930.

Aug. 26. Hearing set Nov. 13, 1930.

Oct. 8. Notice of appearance of Paul E. Shorb as counsel for taxpayer filed.

" 8. Motion to transfer to the Minneapolis, Minn. Circuit Cal. filed by taxpayer.

" 11. Motion granted.

1931.

June 23. Hearing set July 13, 1931, St. Paul, Minn.

July 14. Hearing had before W. C. Lansdon, Div. 8, on the merits.
Submitted. Briefs due in 60 days.

" 31. Transcript of hearing July 14, 1931 filed.

Sept. 4. Brief filed by G. C.

" 8. Brief filed by taxpayer.

1932.

Jan. 12. Opinion rendered, W. C. Lansdon, Div. 8. Decision will be entered for the respondent.

" 14. Decision entered, W. C. Lansdon, Div. 8.

June 30. Stipulation of venue filed.

July 1. Motion to fix amount of bond at a sum not in excess of $15,000.00 filed by taxpayer. (2.)

" 2. Motion denied.

" 12. Supersedeas bond for $26,000.00 approved and ordered filed.

" 13. Petition for review to Court of Appeals of D. C. with assignments of error filed by taxpayer.

" 13. Proof of service filed.

Aug. 26. Motion for extension to 11-13-32 to prepare evidence and transmit record filed by taxpayer.

" 26. Order enlarging time to Nov. 14, 1932 for preparation and delivery of record entered.

Oct. 28. Præcipe filed.

" 28. Proof of service filed.

" 28. Agreed statement of evidence lodged.

" 29. Agreed statement of evidence approved & ordered filed.

2 [Stamp:] United States Board of Tax Appeals. Filed Sep. 9, 1929.

Sept. 9, 1929.

United States Board of Tax Appeals.

Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Petition.

The above named taxpayer hereby enters its appeal from the determination of the Commissioner of Internal Revenue

as set forth in his deficiency letter IT:AR:C-7-CEO-60D dated July 11, 1929, and as a basis of its appeal sets forth the following:

1. The taxpayer is a Minnesota Corporation with its principal office at Duluth, Minnesota.

2. The deficiency letter (copy of which is attached and marked "Exhibit A") was mailed to the taxpayer on July 11, 1929.

3. The taxes in controversy are income taxes for the calendar year 1927 and for $19,005.60.

4. The determination of taxes contained in said deficiency letter is based upon the following error:

Inclusion in the income of taxpayer of an alleged "profit on sale of notes" of the sum of $140,782.20.

5. The facts upon which the petitioner relies as a basis of its appeal are as follows:

During the year 1926 the taxpayer made a sale on the installment basis of all of its assets, receiving therefor a small amount in cash (less than one-fourth the sale price) and a number of notes due annually thereafter. The taxpayer reported the transaction in 1926 as an installment sale under the provisions of Section 212 (d) of the Revenue Act of 1926 and Article 45 of Regulations 69. The installment notes which the taxpayer received for its property were made payable to the order of the taxpayer and were signed by the purchaser. During the year 1927 the taxpayer, solely upon the strength of its own endorsement of said notes and by reason of the personal standing and integrity of its officers and stockholders, were able to discount, and did discount, with full recourse upon itself in case of nonpayment, all of said notes. The taxpayer did not "sell" or "dispose" of said notes, but simply discounted them, or, in every practical sense, borrowed money on them. There were no "payments actually received" during the year 1927 by the taxpayer upon these discounted notes. Consequently, respondent's inclusion of the sum of $140,782.20 of profit on the "sale" of notes is erroneous because there was no sale of any notes. Likewise his determination that

petitioner earned a profit during the year 1927 through
3 its handling of said notes is not supported by the language of Section 212 (d) of the Revenue Act of 1926

which prescribes that, under circumstances similar to these, the taxpayer may "return as income * * * in any tax-

able year the proportion of the installment payments actually received in that year which the total profit realized or to be realized when the payment is completed, bears to the total contract price", because there were no "payments actually received" by petitioner during the year 1927 upon said discounted notes. Petitioner has elected to report this transaction as an installment sale, which is its privelege under the law, and did during the year 1927, and has every year since, reported the proportionate profit upon payments actually received in each year and has paid income tax thereon and will continue to do so until all payments have been actually received, so that respondent will collect the full amount of tax due upon the profit in said transaction from time to time as such taxes become due under the Revenue Acts.

Wherefore the petitioner prays that this Board may hear the proceeding and find that respondent has erred in his inclusion of $140,782.20 in the income of petitioner for the year 1927 as "profit on sale of notes."

FRANK W. WILSON,
FRANK W. WILSON,
Counsel for Petitioner.

514-517 Providence Building, Duluth, Minnesota.

STATE OF MINNESOTA,
County of St. Louis, ss:

J. L. Washburn, being duly sworn, says that he is President of Alworth-Washburn Company the taxpayer named in the foregoing Petition, and as President is duly authorized to verify the foregoing Petition; that he has read said Petition and is familiar with the statements therein contained, and that the facts therein stated are true, except such facts as are stated to be upon information and belief, and those facts he believes to be true.

J. L. WASHBURN.

Subscribed and sworn to before me this 6th day of September, 1929.

[Notarial Seal, St. Louis Co., Minn.]

A. J. NOLAN,
Notary Public.

A. J. Nolan, Notary Public, St. Louis Co., Minn. My commission expires Jan. 30, 1935.

4 "EXHIBIT A."

IT:AR:C-7. CEO-60D.

July 11, 1929.

Alworth-Washburn Company,
1600 Alworth Building,
Duluth, Minnesota.

SIRS:

In accordance with Section 274 of the Revenue Act of 1926, you are advised that the determination of your tax liability for the years 1927 discloses a deficiency of $19,-005.60, as shown in the statement attached.

The section of the law above mentioned allows you to petition the United States Board of Tax Appeals within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested to execute the inclosed Form 866 and forward both original and duplicate to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing of this agreement form will expedite the closing of your return by permitting an early assessment of any deficiencies and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the agreement form, or on the date assessment is made, whichever is earlier; whereas if no agreement is filed, interest will accumulate to the date of assessment of the deficiencies.

Respectfully,

ROB'T H. LUCAS,
Commissioner.

(Signed) C. B. ALLEN,
Deputy Commissioner.

Copy.

5 *Statement.*

IT:AR:C-7. CEO-60D.

In re Alworth-Washburn Company, 1600 Alworth Building, Duluth, Minnesota.

Year.	Corrected tax liability.	Tax liability. Tax previously assessed.	Tax liability. Deficiency.
1927	$25,671.18	$6,665.58	$19,005.60

Reference is made to the report of the Internal Revenue Agent in Charge at St. Paul, Minnesota, covering your income tax liability for 1927 and to your protest filed.

Under date of May 25, 1929, this office advised you of its approval of the revenue Agent's report and the reasons therefor with respect to the contested adjustment of including in income the profit derived from the disposition of notes accepted by you in payment of certain of your assets.

In a letter to this office dated June 15, 1929, your agent, Mr. Frank W. Wilson of your city, while protesting the action of this office, has submitted no new evidence and states that a conference is not desired. Under those circumstances the decision contained in office letter of May 25, 1929, is reaffirmed.

Net income reported on return	$49,374.67
Add: 1. Profit on sale of notes	140,782.20
Net income as adjusted	$190,156.87

Explanation of Adjustment.

1. Taxable income under Article 31, Regulations 69. See prefatory comment.

Computation of Tax.

Net income as adjusted, subject to tax at 13½%	$190,156.87
Tax liability	25,671.18
Tax previously assessed	6,665.58
Deficiency	$19,005.60

6 [Stamp:] United States Board of Tax Appeals. Filed Oct. 24, 1929.

United States Board of Tax Appeals.

Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Answer.

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

1, 2 and 3. Admits the allegations contained in Paragraphs 1, 2 and 3 of the petition.

4. Denies that he erred in determining the tax set forth in said notice of deficiency and further denies that he erred as alleged in Paragraph 4 of the petition.

5. Denies any knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 5 of the petition and therefore denies the same.

6. Denies generally and specifically each and every allegation contained in taxpayer's petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the taxpayer's appeal be denied.

(Signed) C. M. CHAREST,
C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

Of Counsel:
L. A. LUCE,
Special Attorney,
Bureau of Internal Revenue.

k 10-21-29.

7 A true copy. Teste:

[Seal U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk U. S. Board of Tax Appeals.

25 B. T. A., —

United States Board of Tax Appeals.

Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Promulgated January 12, 1932.

Where a corporation sells a group of installment notes, representing the unpaid portions of the purchase price of lands sold by it in a prior year, by blank endorsement to a bank; the amount received by it in said transaction, to the extent that it represents profits realized from the sale of the lands, is reportable as a part of its gross income for the year.

Frank W. Wilson, C. P. A. and *A. C. Washburn, Esq.*, for the petitioner.

A. H. Fast, Esq., for the respondent.

Opinion.

LANSDON:

The respondent has asserted a deficiency in income tax for the year 1927 in the amount of $19,005.60. The petitioner is a Minnesota corporation with principal office at Duluth. It was organized in 1907, for the purpose of acquiring and selling for profit timber lands in the state of Oregon. In 1926 it sold to the Brooks-Scanlon Lumber Company, a corporation, some 12,440 acres, "more or less" of timber lands, for the contract price of $590,900, payable $100,000 in cash at the time of sale and the balance in five equal annual installments of $98,180, payable successively on May 1st of each year thereafter following. These installments were evidenced by five groups of promissory notes drawing 6 per cent interest, and executed in the name of the purchasing corporation in favor of the petitioner. Later, the gross price was adjusted by the parties to $588,838, and the 1926 payments to $121,118.02. This reduced the May 1, 1927 pay-

ment to $75,000, but left the remaining four install-
8 ments as hereinabove stated. In its income tax re-
turn for 1926, the petitioner elected to report the taxable profit realized from the sale of these lands upon the installment basis, and reported $121,118.02 as cash received upon such purchase price in that year. This return was accepted by the Commissioner of Internal Revenue and tax liability settled in conformity therewith.

On May 1, 1927, the petitioner collected $75,000 on the notes then due. On December 6th, following, it discounted the remainder of the installment notes by blank indorsement to the First National Bank of Minneapolis and received $403,882.97 in cash therefor. This amount, less a small portion retained for expenses and tax liabilities, was immediately distributed to petitioner's stockholders and credited in its books as "advances to stockholders." In its income tax return for 1927, the petitioner reported the single installment of $75,000 as the only cash received from the sale of its lands in that year and deferred reporting the price received for the remainder of the installment notes to their respective maturity years. As the notes became due they were paid by the Brooks-Scanlon Lumber Company, maker.

The respondent has held that the installment sale of the petitioner's lands became a closed transaction on December 6, 1927, when it discounted the notes received in payment to the Minneapolis Bank; and, that in virtue thereof, its entire gain was then realized and taxable. The petitioner concedes the respondent's computation of gain, but contends that, for income tax purposes, it should be spread over the years in which the installment notes became due;
that in virtue of its indorsement of the notes, it in-
9 curred a continuing liability to the bank which
ratably deferred its realization of gain until that liability was finally extinguished by their payment. Such a situation, the petitioner contends, makes its relationship with the bank that of a borrower, and the proceeds received a loan which was discharged ratably in the subsequent years of their payment and that it is entitled to continue reporting its income from sale of its timber land on the installment sale basis.

The issue and material facts here are on all fours with those considered by us in *Grace T. Mytinger,* 4 B. T. A. 896 and *Packard Cleveland Motor Co.,* 14 B. T. A. 118, in each of which we held contrary to the contentions of the petitioner. In our opinion such decisions are controlling here. *Cf. Lucius H. Elmer,* 22 B. T. A. 224. The facts in the instant proceeding, however, are even more strongly against the theory advanced by the petitioner than in the cases cited, since its own evidence discloses that the parties concerned treated the discounting of the notes as a sale and not a loan. In this connection we need only to refer to the minutes of the directors' meeting where the transaction was discussed and the "sale" ratified, and to the fact that the proceeds received from the bank were immediately distributed to the stockholders. The testimony of an official of the discounting bank negatives any theory or understanding that the amount paid for these notes was treated as a loan to petitioner. He admitted, under cross examination, that at no time was there an existing debt or obligation which the petitioner could "pay off" and get these notes back; that (quoting his exact words) "We were under no obligation to return the notes to them and accept money before maturity" * * * "They are our notes, if we discounted them". The petitioner's attempts to show through bookkeeping entries a contrary intent, does
10 not change the true character of the transaction considered. Bookkeeping entries cannot prevail over facts. *Doyle* v. *Mitchell Bros. Co.,* 247 U. S. 179; *Chicago, Rock Island & Pacific Railway Co.,* 13 B. T. A. 988; *Kansas City Southern Railway Co.,* 16 B. T. A. 665; *Terminal Railway Association,* 17 B. T. A. 1135.

Decision will be entered for the respondent.

11 United States Board of Tax Appeals, Washington.

Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Decision.

Pursuant to the determination of the Board, as set forth in its report promulgated January 12, 1932, it is

Ordered and decided that there is a deficiency of $19,005.60 for the year 1927.

Enter.

(Signed) W. C. LANSDON,
Member.

Entered Jan. 14, 1932.

A true copy. Teste:

[Seal U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk U. S. Board of Tax Appeals.

12 [Stamp:] United States Board of Tax Appeals. Filed Jun. 30, 1932.

United States Board of Tax Appeals.

Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Agreement for Review by the Court of Appeals of the District of Columbia.

It is stipulated and agreed between the parties to these proceedings by their respective undersigned attorneys, that pursuant to the provisions of Section 1002 (d) of the Revenue Act of 1926, the decision of the United States Board of Tax Appeals in the above described proceedings may be reviewed by the Court of Appeals of the District of Columbia.

PAUL E. SHORB,
PAUL E. SHORB,
701 *Union Trust Building,*
Washington, D. C.,
Counsel for Petitioner.

C. M. CHAREST,
C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue,
Counsel for Respondent.

13 [Stamp:] United States Board of Tax Appeals. Filed Jul. 13, 1932.

United States Board of Tax Appeals.

Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Petition for Review of Decision by the United States Board of Tax Appeals by the Court of Appeals of the District of Columbia.

The above-named petitioner, Alworth-Washburn Company, is aggrieved by decision of the United States Board of Tax Appeals rendered against it on January 14, 1932, in the case of Alworth-Washburn Company v. Commissioner of Internal Revenue, No. 45651, on the docket of the Board, and respectfully submits its Petition for Review thereof by the Court of Appeals of the District of Columbia, pursuant to a stipulation entered into by the parties under the provisions of Section 1002 (d), Revenue Act of 1926, 44 Stat. 110, that review shall be by said Court, which stipulation was filed with the Clerk of said Board of Tax Appeals. For cause, the petitioner respectfully shows as follows:

14 Statement of Nature of the Controversy.

1. Petitioner is a Minnesota corporation with principal office at Duluth, Minnesota. On July 11, 1929, the respondent, Commissioner of Internal Revenue, determined a deficiency in income taxes against the petitioner for the calendar year 1927 in the amount of $19,005.60. On September 9, 1929, the petitioner filed with the United States Board of Tax Appeals its petition for redetermination of said deficiency. The respondent thereafter duly filed his answer to petitioner's petition.

2. The sole question in controversy before the Board of Tax Appeals was whether petitioner, by discounting certain installment notes in 1927 which it had received prior thereto, thereby forfeited the right to report the income reflected in said notes in later years. The petitioner was organized in 1907 for the purpose of acquiring timber and then holding said timber en-bloc for the purpose of sale rather than for

operation. In 1926 the petitioner made a sale on the installment plan of all of its capital assets to the Brooks-Scanlon Lumber Company for $588,838.02, petitioner receiving cash and notes of the Brooks-Scanlon Lumber Company. The profit from said sale was reported on the installment basis in petitioner's tax return for the year 1926, and the respondent agreed that petitioner correctly reported the income from said sale on the installment basis.

No dispute exists as to the total amount of profit re-
15 sulting from the sale of said timber.

During 1927 petitioner discounted the installment notes due in 1928, 1929, 1930 and 1931 received from Brooks-Scanlon Lumber Company, with the First National Bank of Minneapolis endorsing said notes with unqualified endorsements, thereby guaranteeing payment at maturity. After it had discounted its installment notes receivable, petitioner continued to report the profit from the sale of said timber to Brooks-Scanlon Lumber Company on the installment basis and continued its corporate existence for that reason and because of its liability as endorser on said discounted notes. Petitioner has reported on the installment basis all the profit represented in said notes and paid taxes thereon. During the years 1928, 1929, 1930 and 1931, petitioner's only material income consisted of such installment income as it realized upon actual payment of said installment notes receivable as they became due throughout said years. During said years petitioner incurred certain corporate expenses, consisting of license fees payable to certain states, audit expenses, and miscellaneous expenses.

The Commissioner of Internal Revenue held that the installment sale of petitioner's timber became a closed transaction on December 6, 1927, when petitioner discounted the Brooks-Scanlon Lumber Company notes with the First National Bank of Minneapolis, and that its entire gain was then realized and taxable. The petitioner, on the con-
16 trary, contended that discounting of said installment notes in 1927 did not forfeit petitioner's right to report profit reflected in said notes, in later years when actually paid, and that petitioner correctly reported said profit in the years 1928 to 1931, inclusive.

3. Under date of January 12, 1932, the Board of Tax Appeals promulgated its opinion, reported at 25 B. T. A. 140. The Board held that petitioner sold said Brooks-Scanlon

Lumber Company notes to the First National Bank of Minneapolis in 1927 and the profit represented in said notes constituted taxable income in said year. Thereafter, on January 14, 1932, the Board entered its formal decision redetermining the deficiency to be $19,005.60, the same amount as proposed by respondent.

Assignments of Error.

The petitioner believes and avers that errors were committed by the Board to its damage and prejudice as follows:

1. In entering judgment for respondent.
2. In failing to enter judgment for petitioner.
3. In redetermining the deficiency as $19,005.60 for the year 1927.

17 4. In holding and deciding that the discounting of notes constitutes a sale of notes instead of a loan by the discounting bank.

5. In holding and deciding that the installment sale of petitioner's timber became a closed transaction on December 6, 1927, when petitioner discounted the Brooks-Scanlon Lumber Company notes with the First National Bank of Minneapolis.

6. In holding and deciding that the taxable profit on the sale of petitioner's timber to Brooks-Scanlon Lumber Company could be determined in the year 1927.

7. In holding and deciding that petitioner actually received "payments" when it discounted the Brooks-Scanlon Lumber Company notes in 1927.

8. In failing to hold and decide that proper and approved standard methods of accounting did not permit the determination of any profit when petitioner discounted said Brooks-Scanlon Lumber Company notes to the First National Bank of Minneapolis.

9. In finding and holding that the petitioner sold the Brooks-Scanlon Lumber Company notes to the First National Bank of Minneapolis on December 6, 1927, because such finding is not supported by and is contrary to the evidence adduced at the hearing before the Board.

18 10. In finding and holding that the transaction between petitioner and the First National Bank of Minneapolis, to which it endorsed said Brooks-Scanlon Lumber Company notes, did not constitute the loan of money by said bank to the petitioner with the notes trans-

ferred as collateral, because said finding is not supported by and is contrary to the evidence adduced at the hearing before the Board.

11. In holding and deciding that the petitioner realized taxable income in 1927 from its transfer of Brooks-Scanlon Lumber Company notes to the First National Bank of Minneapolis.

12. In failing to find and hold that the transaction between the petitioner and the First National Bank of Minneapolis, to which it endorsed the Brooks-Scanlon Lumber Company notes, constituted the loaning of money by said bank to the petitioner with the notes transferred as collateral, as was established by the evidence adduced at the hearing held before the Board.

13. In failing to hold and decide that the petitioner realized no taxable income from its transfer of the Brooks-Scanlon Lumber Company notes to the First National Bank of Minneapolis in 1927.

14. In failing to hold and decide that the petitioner correctly reported the profit represented in said Brooks-Scanlon Lumber Company notes in the years subsequent to 1927, when said Lumber Company actually paid said notes.

19 15. Wherefore, your petitioner prays that the decision of the United States Board of Tax Appeals, entered herein against it, be reviewed and reversed by the Court of Appeals of the District of Columbia and that the Clerk of the Board of Tax Appeals be directed to transmit and deliver to the Clerk of said Court certified copies of all the documents necessary and material to the presentation and consideration of the foregoing Petition for Review, and as required by the rules of said Court and statutes made and provided; and your petitioner prays for such other and further relief as the Court may deem proper in the premises.

PAUL E. SHORB,
PAUL E. SHORB,
M. P. WORMHOUDT,
M. P. WORMHOUDT,
Attorneys for Petitioner.

COVINGTON, BURLING & RUBLEE,
701 *Union Trust Building,*
Washington, D. C.,
Of Counsel.

20 DISTRICT OF COLUMBIA, *ss:*

Paul E. Shorb, being duly sworn, says that he is attorney-of-record for the petitioner, Alworth-Washburn Company, and as such is duly authorized to verify the above and foregoing Petition for Review to the Court of Appeals of the District of Columbia; that he has read said Petition for Review and is familiar with the statements therein contained; and that the facts therein stated are true, except such facts as may be stated on information and belief, and those facts he believes to be true.

PAUL E. SHORB.

Subscribed and sworn to before me this 5th day of June, 1932.

[Seal of Pearl M. Hauser, Notary Public, District of Columbia.]

PEARL M. HAUSER,
Notary Public.

21 [Stamp:] United States Board of Tax Appeals. Lodged Oct. 28, 1932.

[Stamp:] United States Board of Tax Appeals. Filed Oct. 29, 1932.

United States Board of Tax Appeals.

B. T. A. Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Statement of Evidence.

The above cause came on for hearing before the Honorable W. C. Lansdon, member of the United States Board of Tax Appeals, upon the fourteenth day of July, 1931, at St. Paul, Minnesota, there being present the Petitioner by its counsel, Frank W. Wilson, C. P. A., and A. C. Washburn, Esquire, and Respondent by his counsel, A. H. Fast, Esquire.

Mrs. Helen McComber, called as a witness by and on behalf of the Petitioner, after being duly sworn, testified as follows:

(Direct Examination:)

My home is in Duluth, Minnesota. I have lived there for a number of years. I know the Alworth-Washburn Company, the Petitioner in this case. I am an officer of that company holding the office of Assistant Secretary. I was first elected to that office in 1923 and have held that office continuously since that time. I am familiar with a
22 sale or contract for sale which was entered into in 1926 between the Alworth-Washburn Company and the Brooks-Scanlon Lumber Company involving a sale by Alworth-Washburn Company of a large block of timber land.

The Petitioner by its counsel, Mr. Wilson, thereupon offered in evidence and there was received in evidence without objection as Petitioner's Exhibit No. 1 copy of the contract entered into in 1926 between the Alworth-Washburn Company and the Brooks-Scanlon Lumber Company. Said exhibit is attached hereto and incorporated in and made a part of this Statement of Evidence.

Counsel for Petitioner and Respondent then orally agreed that by reason of acreage the sales price of $590,900 was later on reduced and determined to be $588,838.02.

Petitioner by its counsel thereupon offered in evidence and there was received in evidence without objection as Petitioner's Exhibit No. 2, one of the serial notes taken by Petitioner under said contract of sale, Petitioner's Exhibit No. 1. Said exhibit is attached hereto and incorporated in and made a part of this Statement of Evidence.

Counsel for Petitioner and Respondent agreed that this is one of the series of notes received in settlement of the transaction between the Alworth-Washburn Company and the Brooks-Scanlon Lumber Company, the due dates and the amounts of the notes being set out in the contract (Petitioner's Exhibit No. 1).

23 Petitioner by its counsel offered in evidence certified copies of Petitioner's original and amended income tax returns for the year 1926, income tax return for

the year 1928, income tax return for the year 1929, and retained copy of income tax return for the year 1930. Said returns were received in evidence without objection as Petitioner's Exhibits Nos. 3, 4, 5 and 6, respectively. Said exhibits are attached hereto, incorporated herein, and made a part of this Statement of Evidence.

There was then offered and received in evidence as Joint Exhibit A-7 copy of Petitioner's original return for the calendar year 1927. Said exhibit is attached hereto, incorporated herein, and made a part of this Statement of Evidence.

Counsel for Petitioner and Respondent orally agreed that the purpose of the Alworth-Washburn Company in acquiring timber was to hold it en bloc, to sell it rather than to operate it, and to make a block sale at the earliest possible moment.

There being no cross-examination of the witness McComber, she was thereupon excused.

24 **Julius S. Pomeroy**, called as a witness by and on behalf of the Petitioner, after being duly sworn, testified as follows:

(Direct examination:)

I am and have been for a number of years Vice-President and an active officer of the First National Bank in Minneapolis. I have acted in that capacity long before the year 1926.

I have some personal knowledge of the discount in 1927 of the notes of the Brooks-Scanlon Lumber Company to the Alworth-Washburn Company. I have refreshed my recollection by examining the records of the bank in connection with that transaction. The notes I have referred to were all similar to the one marked Petitioner's Exhibit No. 2 except that they were different maturities. They were in a series.

This card is one of the original records of the bank—it is what we call a liability ledger card. This card for this particular customer is similar to other cards for each respective customer of the bank who was obligated to us in any manner. The cards do not differ as the obligation differs. They are all alike. This card is for the Alworth-

Washburn Company. I can tell from the card that the date of the opening of that account was December 6, 1927. That date corresponds with the date we discounted these notes of the Brooks-Scanlon Lumber Company. That date was December 6, 1927. The record shows that we discounted paper aggregating $392,720 for the Alworth-Wash-
25 burn Company, the paper consisting of notes made by the Brooks-Scanlon Lumber Company. If we had all of the cards like this in the bank collected together and the total added up, it would show bills discounted by the First National Bank. In banking parlance this means the same thing as loans made. The aggregate of the footings on those cards would show the amount of paper that the bank had under discount in banking parlance. It would show their loans and discounts, that is the total of it on their books as loans and discounts.

Petitioner by its counsel thereupon offered in evidence and there was received in evidence as Petitioner's Exhibit No. 8 the card record of the First National Bank of Minneapolis referred to by the witness. Said exhibit is attached hereto, incorporated herein and made a part of this Statement of Evidence.

Referring again to Petitioner's Exhibit No. 8, the first column has reference to the date on which we discounted the notes, being December 6, 1927. The next column headed "Number" is the number of the note on our journal record; these numbers run continuously. The next column is entitled "Maker or Endorser". The purpose of this column is that if these notes, for example, were notes of the Alworth-Washburn Company, and they have some personal endorsement or corporate endorsement, that endorser would be listed here. If they are notes of another company discounted for the Alworth-Washburn Company, then the name of the maker appears. There is nothing on
26 the card to indicate whether the Brooks-Scanlon Lumber Company, whose name is listed in that column, is the maker or endorser of the note. There is on the original record but not on the card. The next column is the due date of the respective notes and the next column is the date on which it was paid. The next column is the amount of each note and the next column entitled "Credit" is that wherein we enter the amounts of payment as made.

We have a column here entitled "Collateral Line". It indicates that there was some collateral in connection with the transaction. We would refer to the collateral record to see what it was. I have the collateral record here with me. This is the collateral record showing that on December 21, 1927, we received a warranty deed or agreement for sale on timber land in connection with this loan. All that happened was that the deed for this land was placed in escrow. The notes were secured by the deed as collateral.

If the Alworth-Washburn Company instead of offering or tendering us these notes for discount had borrowed money from us upon their note and had deposited these Brooks-Scanlon notes therein as collateral to their loan, the record (Petitioner's Exhibit No. 8) would have been headed in the same way but it would simply have been a description of that note of Alworth-Washburn Company and we would have had in our collateral record like that card a list of the Brooks-Scanlon Lumber Company notes. If the notes had not been paid the bank would have looked for payment
to the Alworth-Washburn Company. It would have
27 made no difference to the bank nor would the bank
have made any different decision in the acceptance of this paper if a loan had been made by the Alworth-Washburn Company, secured by the Brooks-Scanlon notes, that is their note with the Brooks-Scanlon notes as security. So far as the bank was concerned the transaction would be identical.

During this period the bank had a line of credit extended to the Brooks-Scanlon Lumber Company. These Brooks-Scanlon notes shown upon the card (Petitioner's Exhibit No. 8) were not applied against that line of credit. In other words, they would have been permitted their entire line of credit in addition to any of their obligations on these notes. I do not know whether they did or not. The Alworth-Washburn Company did not have any agreement or contract with the bank other than that created by the endorsement of this paper.

From time to time upon call of the Examiner the bank shows a statement of its assets and liabilities. One of the items of assets that always appears is loans and discounts. That indicates the amount of money the bank had loaned direct to customers and discounted paper for them. It includes any paper which represents an obligation due the

bank. The Alworth-Washburn or these Brooks-Scanlon notes that required endorsement would be included in that statement of assets and under that head. If that were broken down we would have the same result in it as to pertinent portions—this account of Alworth-Washburn Company, represented by the card which I hold (Petitioner's Exhibit No. 8) would be one of those com-
28 ponent parts.

(Cross-examination:)

These notes of the Brooks-Scanlon Company were discounted in our bank by the payee, Alworth-Washburn Company, in the regular way. Anybody else bringing notes that we cared to discount would have been treated in the same way. The bankers have a regular way for loans and then discounting notes. If we wish to make a direct loan instead of rediscounting some paper, the Alworth-Washburn Company would sign a note and we would have a note evidencing indebtedness of some kind in our bank. In this instance, the Alworth-Washburn Company signed no note. They endorsed these notes and we discounted them.

I presume the Alworth-Washburn Company could have made arrangements with us to take these notes if agreeable to us. We were under no obligation to return the notes to them and accept money before maturity but they might have concluded a transaction by which they could pay us money and return the notes to them. They are our notes if we discount them. The Alworth-Washburn Company were on these notes as endorsers.

Q. If the Brooks-Scanlon Lumber Company would have failed to pay these notes, or if you could not have realized the proceeds from the loan, then you would have called upon Alworth-Washburn Company as endorser, is that correct? A. We would not have done anything with the loan. If the Brooks-Scanlon Company had not paid the notes we would have notified the Alworth-Washburn Company and asked them to take them up.

29 Q. In that event you would have notified the Alworth-Washburn Company? A. Yes.

(Redirect examination:)

In the case of any default whatever we would have immediately demanded that the Alworth-Washburn Company

pay us for the notes. We would not have proceeded against Brooks-Scanlon Company.

If we had been willing to, and did take these notes from Alworth-Washburn Company without recourse, we would have entered the transaction on our books on either Brooks-Scanlon Company or Alworth-Washburn Company. It would have been an entirely different entry from this. In that case the amount of indebtedness would have been added to other indebtedness of Brooks-Scanlon Company in determining whether their line of credit was exhausted or not.

I think I should answer that for the purpose of understanding of the Court that we do not purchase notes of customers of ours who have lines of credit because any purchase of such paper and putting it on our books is unfair to them because it immediately upsets the credit which we have at our disposal, so that we do not buy outright paper of a customer although we frequently discount it for other people. This is a mere matter of policy. We do buy paper on the open market from brokers on which there is no recourse at all upon the sellers of the paper. We look to the maker of the note and we call that buying paper in the commercial paper market from brokers as distinguished from this character of transaction.

30 If the Alworth-Washburn Company had had a line of credit with us, these notes which we discounted in 1927 would not have been applied against the exhaustion of that open unsecured line of credit because it is an obligation of another person that we discounted for them. We do not figure that against their direct line. For example, we will frequently give a concern a direct line of half a million dollars and an indirect line of another half a million of paper we discount for them.

(Witness excused.)

Counsel for Petitioner and Respondent thereupon agreed that the sale in 1926 constituted the remainder of Petitioner's assets.

Frank W. Wilson, called as a witness by and on behalf of the Petitioner, after being duly sworn, testified as follows:

(Direct examination:)

I am an accountant by profession. I have practiced for a considerable number of years and have specialized largely in income tax work. I have had charge of the keeping of the books or the supervision of the books of a number of corporations whose income tax matters are more or less complicated. I have had charge of or supervision of the books of the Alworth-Washburn Company during the year here in question. I am familiar with their books and accounts and how they are carried and their statements made out from time to time.

I have had supervision of the preparation of their
31 income tax returns during the year 1926 and subsequent years. I supervised that work—the men in my office did the detail work. I know what other assets, if any, remained in the Alworth-Washburn Company after the disposal of the timber to the Brooks-Scanlon Company. Referring particularly to the Joint Exhibit A-7, the only other asset from that involved in these notes receivable after the sale of 1926 was cash retained in bank, which it was estimated was sufficient to care for the obligations of the corporation. The 1927 statement shows cash in bank at the end of the year, $51,482.39. These notes receivable which had been discounted were carried as assets on the corporation's books even after they had been discounted. I carried a corresponding liability on the same notes. The proceeds of the notes would be recorded in cash-on-hand less whatever distributions had been made.

The company was called on by the bank it did business with from year to year to produce financial statements. The notes here in question have been carried on the books and the bank entries, and income tax returns, and interest statements as liabilities throughout down to the present time. They have been carried in the amount of the unpaid balances thereon and the corresponding asset has been carried on the asset side or notes receivable.

Subsequent to the year 1927 the average operating expenses of the company totaled about $1500 per year, made up of license fees payable to a state or certain states and
some expenses in connection with the handling of
32 this tax matter. We might refer to it as audit expenses. The company has had some little secretarial

costs and possibly some postage and stationery, totalling about $15 per year on the average.

The functions performed by the corporation during these years have been to inquire from time to time as to the payment of these notes by the makers, to prepare income tax returns to the Federal Government, and to prepare certain returns to various states which have been required. In Oregon they require corporation returns and Minnesota has recently had some such requirements.

When these notes were disposed of the proceeds were distributed to the stockholders in the ratio of their stockholdings. We retained an amount in cash to meet any possible liabilities. The distribution was immediately made of the proceeds of these notes which were discounted and of all the money belonging to the company, except the sum which was considered sufficient to take care of income tax obligations and other obligations of the corporation owing on the books of the Alworth-Washburn Company. As such distributions were charged as advances to stockholders and that is also an asset in the books of Alworth-Washburn Company which I did not mention a moment ago. That appears on the balance sheet in this Joint Exhibit. They charged the amount turned over to the stockholders to the stockholders themselves because they would have to pay that money back if the makers of these notes had defaulted.

33 Q. So you at all times protected yourself in your ability to take these notes out from the First National Bank in Minneapolis, if that necessity arose? A. It has been my object to keep the corporation in a position to take care of its obligations.

(Cross-examination:)

Q. Of course, the books were kept under your supervision and the bookkeeping entries were made in accordance with your theories of the nature of this transaction? A. I determined the entries in every instance except certain small transactions that did not amount to anything.

(Witness excused.)

Counsel for Petitioner and Respondent orally agreed that the notes were in each instance all paid on their due date.

Counsel for Respondent thereupon introduced in evidence and there was received in evidence without objection as Respondent's Exhibit B copy of the minutes of the directors' meeting of the Alworth-Washburn Company held on December 10, 1927. Said exhibit is attached hereto, incorporated herein, and made a part of this Statement of Evidence.

Thereupon Petitioner and Respondent rested their case, no other witnesses being called by either Respondent or Petitioner.

The Petitioner and the Respondent by their respective counsel agree that the Clerk of the United States
34 Board of Tax Appeals shall make photostatic or typewritten copies of the aforementioned Petitioner's Exhibits Nos. 1, 2, 3, 4, 5, 6 and 8, Joint Exhibit A-7 and Respondent's Exhibits Nos. — and B, and include them in the record of this proceeding.

The foregoing evidence is all of the material evidence adduced at the hearing before the Board of Tax Appeals and the same is approved by the undersigned as attorneys for the Petitioner, Alworth-Washburn Company.

PAUL E. SHORB,
PAUL E. SHORB,
M. P. WORMHOUDT,
M. P. WORMHOUDT,
Attorneys for Petitioner.

The foregoing evidence is all of the material evidence adduced at the hearing before the Board of Tax Appeals and the same is approved by C. M. Charest, General Counsel, Bureau of Internal Revenue, as attorney for the Commissioner of Internal Revenue.

C. M. CHAREST,
C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

Approved and ordered filed this *day of 1932* October 29, 1932.

W. C. LANSDON,
Member U. S. Board of Tax Appeals.

35 U. S. Board of Tax Appeals, Div. 8.

Docket 45651.

PETITIONER'S EXHIBIT 1.

Admitted in Evidence Jun. 14, 1931.

This agreement, made and entered into this first day of May, A. D. 1926, by and between *Alworth-Washburn Company,* a corporation organized under the laws of the State of Minnesota, with its principal place of business at Duluth, Minnesota, but also duly qualified to do and transact business in the State of Oregon, as party of the first part, and *Brooks-Scanlon Lumber Company,* a corporation also organized under the laws of the State of Minnesota, and duly qualified to do and transact business in the State of Oregon, and having its principal place of business at Minneapolis, Minnesota, as party of the second part,

Witnesseth:

That the said Alworth-Washburn Company in consideration of the payments to be made by, and the covenants and agreements of the said Brooks-Scanlon Lumber Company as herein stated, hereby sells and agrees to convey to the said Brooks-Scanlon Lumber Company, its successors, or assigns, by deed of warranty upon the prompt and full performance by the said Brooks-Scanlon Lumber Company of its part of this agreement, the lands and premises
36 situated in the County of Jefferson and State of Oregon, described on the schedule marked "Schedule A" hereto attached and made a part of this agreement, and aggregating in all Twelve Thousand Four Hundred Forty (12,440) acres more or less, according to Government Survey, which lands are also designated and colored in red upon the map or diagram initialed "J. L. W." and "M. J. S.", hereto attached and made a part of this agreement.

The said Brooks-Scanlon Lumber Company, in consideration of the premises, hereby agrees to pay to the said Alworth-Washburn Company as and for the purchase price of said premises the sum of Five Hundred Ninety Thou-

sand Nine Hundred Dollars ($590,900.00), in manner and at the times following, to wit:

One Hundred Thousand Dollars ($100,000.00) cash at the ensealing of this instrument, the receipt of which is hereby acknowledged;

Ninety-eight Thousand One Hundred Eighty Dollars ($98,180.00) on May 1, 1927;

Ninety-eight Thousand One Hundred Eighty Dollars ($98,180.00) on May 1, 1928;

Ninety-eight Thousand One Hundred Eighty Dollars ($98,180.00) on May 1, 1929;

Ninety-eight Thousand One Hundred Eighty Dollars ($98,180.00) on May 1, 1930;

Ninety-eight Thousand One Hundred Eighty Dollars ($98,180.00) on May 1, 1931;

together with interest upon all of said deferred payments at the rate of five per cent (5%) per annum, payable
37 annually, from and after said date, all of said obligations being evidenced by the promissory notes of the said Brooks-Scanlon Lumber Company bearing even date herewith and payable to the order of the said Alworth-Washburn Company at the Northern National Bank of Duluth, Minnesota, each and all being payable on or before maturity, such notes being in such denominations as aggregate the above amounts at the maturities above mentioned.

The Alworth-Washburn Company represents and guarantees that it has paid all of the taxes levied and assessed against said premises for the year 1925, and that there are no prior unpaid taxes upon said premises, and it is agreed that all taxes levied, assessed or payable hereafter on said premises shall be paid by the said Brooks-Scanlon Lumber Company.

It is mutually understood and agreed that the chief value of said lands is in the timber thereon, and that no timber shall be cut or removed from said lands or any part thereof prior to the full payment of the said purchase price, except on the following terms and conditions: Should the Brooks-Scanlon Lumber Company desire to cut any timber upon any of the lands before payment in full of the said purchase price, it shall notify the Alworth-Washburn Company

in writing in advance of any cutting which it may desire to do, specifying the particular subdivision or subdivisions of land according to Government descriptions and
38 not less than one government subdivision at any one time, from which it desires to cut timber, and shall make payment to apply on the next payment to fall due under this contract at the rate of Forty Seven and 50/100 Dollars ($47.50) per acre for the land included in said subdivision or subdivisions which it desires to cut, and said Brooks-Scanlon Lumber Company shall only enter or be entitled to enter upon said descriptions so designated to cut the same after such written notification and payment, *provided however,* that such payment shall be waived until payments which may have been made in excess of the cash payment of One Hundred Thousand Dollars ($100,000.00) first specified in this contract shall have been exhausted by such cutting or designations for cutting.

Upon payment of the whole purchase price, the said Alworth-Washburn Company shall execute and deliver to the said Brooks-Scanlon Lumber Company its good and sufficient warranty deed in accordance with the laws of the State of Oregon, warranting the title to said premises, except as to matters arising by reason of the acts or omissions of the said Brooks-Scanlon Lumber Company subsequent to the date of this contract.

Should default be made in the payment of the said several sums of money or any part thereof, or in the payment of said interest or taxes or any part thereof, or in any of the covenants herein to be by the said Brooks-Scanlon Lumber Company kept or performed, then this agree-
39 ment shall be void at the election of the said Alworth-Washburn Company, but not otherwise, and the moneys paid thereunder shall be retained as damages for the non-fulfillment of this contract, and in case of default by the said Brooks-Scanlon Lumber Company in whole or in part, in any or either of the covenants of this agreement to be by it kept and performed, it hereby agrees upon demand of the said Alworth-Washburn Company, quietly and peaceably to surrender possession of said premises and every part thereof, it being understood that until such default the said Brooks-Scanlon Lumber Company is to have possession of said premises, and an agreement which

is to be deemed as supplementary to this agreement and not in contradiction therewith shall be executed between the parties hereto, by the recordation of which notice shall be given to the world of the purchase and possession of said premises by the said Brooks-Scanlon Lumber Company.

In testimony whereof, the parties hereto have caused their respective corporate names and seals to be hereunto affixed by their respective executive officers duly authorized thereto, all in duplicate.

ALWORTH-WASHBURN COMPANY,
(Sgd.) By J. L. WASHBURN,
Its President, and
(Sgd.) PHILIP L. RAY,
Its Secretary.
BROOKS-SCANLON LUMBER COMPANY,
(Sgd.) By D. F. BROOKS,
Its President, and
(Sgd.) H. W. DAVIS,
Its Ass't Secretary.

Signed, sealed and delivered in presence of:
(Sgd.) VENDLA ERICSON.
(Sgd.) WILLIAM C. FLINN.
(Sgd.) J. VICTOR JAEGER.
(Sgd.) W. M. DONALD.

40 STATE OF MINNESOTA,
County of St. Louis, ss:

On this 7th day of May, 1926, before me appeared J. L. Washburn and Philip L. Ray, to me personally known, who, being duly sworn did say that they are respectively the President and Secretary of Alworth-Washburn Company, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and said J. L. Washburn and Philip L. Ray acknowledged said instrument to be the free act and deed of said corporation.

In testimony whereof I have hereunto set my hand and affixed my official seal this the day and year first in this, my certificate, written.

(Sgd.) ROGER D. KEMPTON,
ROGER D. KEMPTON,
Notary Public, St. Louis County, Minn.

My commission expires May 22, 1931.

STATE OF MINNESOTA,
County of Hennepin, ss:

On this 15th day of May, 1926, before me appeared D. F. Brooks and H. W. Davis, to me personally known, who being duly sworn, did say that they are respectively
41 the President and Assistant Secretary of Brooks-Scanlon Lumber Company, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and said D. F. Brooks and H. W. Davis acknowledged said instrument to be the free act and deed of said corporation.

In testimony whereof I have hereunto set my hand and affixed my official seal this the day and year first in this, my certificate, written.

(Sgd.) G. W. DAVIS,
G. W. DAVIS,
Notary Public, Hennepin County, Minn.

My commission expires July 27th, 1932.

42 *Schedule A Attached to Contract Between Alworth-Washburn Company and Brooks-Scanlon Lumber Company, Dated May 1, 1926, and Containing Description of Lands in Jefferson County, Oregon, Covered by said Contract of Purchase.*

Lands in Township Twelve South, of Range Ten East.

The South Half of the South West Quarter (S. ½ of S. W. ¼) and West Half of the South East Quarter (W. ½ of S. E. ¼) of Section Thirteen (13);

The South Half of the South West Quarter (S. ½ of S. W. ¼) of Section Twenty-one (21);

The South Half of the North East Quarter (S. ½ of N. E. ¼), the South Half of the South West Quarter (S.

½ of S. W. ¼), and all of the South East Quarter (S. E. ¼) of Section Twenty two (22);

The entire North Half (N. ½), the North West Quarter of the South West Quarter (N. W. ¼ of S. W. ¼), the North East Quarter of the South East Quarter (N. E. ¼ of S. E. ¼), and the South Half of the South Half (S. ½ of S. ½) of Section Twenty-Three;

All of Section Twenty four (24) except the South East Quarter of the North West Quarter (S. E. ¼ of N. W. ¼) thereof;

All of Section Twenty five (25) except the South Half of the South East Quarter (S. ½ of S. E. ¼) thereof;

The East Half of the North East Quarter (E. ½ of N. E. ¼), the South West Quarter of the North East Quarter (S. W. ¼ of N. E. ¼), the East Half of the North West Quarter (E. ½ of N. W. ¼), all of the South West Quarter (S. W. ¼), the North half of the South East Quarter (N. ½ of S. E. ¼), and the South West Quarter of the South East Quarter (S. W. ¼ of S. E. ¼) of Section Twenty six (26);

43 The West Half of the North West Quarter (W. ½ of N. W. ¼), and all of the South West Quarter (S. W. ¼) of Section Twenty Seven (27);

The entire East Half (E. ½) and the North Half of the North West Quarter (N. ½ of N. W. ¼) of Section Twenty eight;

The North East Quarter (N. E. ¼) and the entire South Half (S. ½) of Section Thirty three (33);

The North West Quarter (N. W. ¼) of Section Thirty four (34);

The entire North Half (N. ½) and the South East Quarter (S. E. ¼) of Section Thirty five;

Lands in Township Thirteen South of Range Ten East.

All of Section One (1) except the North Half of the North East Quarter (N. ½ of N. E. ¼) and the South East Quarter of the North East Quarter (S. E. ¼ of N. E. ¼) thereof;

The North East Quarter of the North East Quarter (N. E. ¼ of N. E. ¼) and the South Half of the North Half (S. ½ of N. ½) of Section Two (22);

The South Half of the North Half (S. ½ of N. ½) of Section Three (3);

The North East Quarter (N. E. ¼) and the South Half of the South Half (S. ½ of S. ½) of Section Five (5);

The North East Quarter (N. E. ¼) of Section Six, (6);

The South Half of the North East Quarter (S. ½ of N. E. ¼) of Section Seven (7);

The North East Quarter of the North West Quarter (N. E. ¼ of N. W. ¼) of Section Eight (8);

The South East Quarter (S. E. ¼) of Section Nine (9);

The South West Quarter (S. W. ¼) of Section Ten (10);

44 The North West Quarter (N. W. ¼) and the South East Quarter (S. E. ¼) of Section Eleven (11);

The North Half of the North East Quarter (N. ½ of N. E. ¼), the South West Quarter of the North East Quarter (S. W. ¼ of N. E. ¼), all of the North West Quarter (N. W. ¼), the North East Quarter of the South West Quarter (N. E. ¼ of S. W. ¼), and the North West Quarter of the South East Quarter (N. W. ¼ of S. E. ¼) of Section Twelve (12);

The South East Quarter (S. E. ¼) of Section Fourteen (14);

The South East Quarter (S. E. ¼) and the entire West Half (W. ½) of Section Seventeen (17);

The North East Quarter (N. E. ¼) of Section Twenty (20);

The North West Quarter (N. W. ¼) and the South East Quarter (S. E. ¼) of Section Twenty two (22);

The North East Quarter of the South West Quarter (N. E. ¼ of S. W. ¼), the North West Quarter of the South East Quarter (N. W. ¼ of S. E. ¼) and the South Half of the South East Quarter (S. ½ of S. E. ¼) of Section Twenty eight (28);

The entire East Half (E. ½) and the East Half of the West Half (E. ½ of W. ½) of Section Thirty (30);

The North Half of the North East Quarter (N. ½ of N. E. ¼), the South East Quarter of the North East Quarter (S. E. ¼ of N. E. ¼) and the North East Quarter of the South East Quarter (N. E. ¼ of S. E. ¼) of Section Thirty four (34).

Lands in Township Twelve South of Range Eleven East.

The North West Quarter of the North West Quarter (N. W. ¼ of N. W. ¼) and the entire South Half (S. ½) of Section Nineteen (19);

5858

Alworth-Washburn Co.
vs.
David Burnet Com. & c.

DIAGRAM

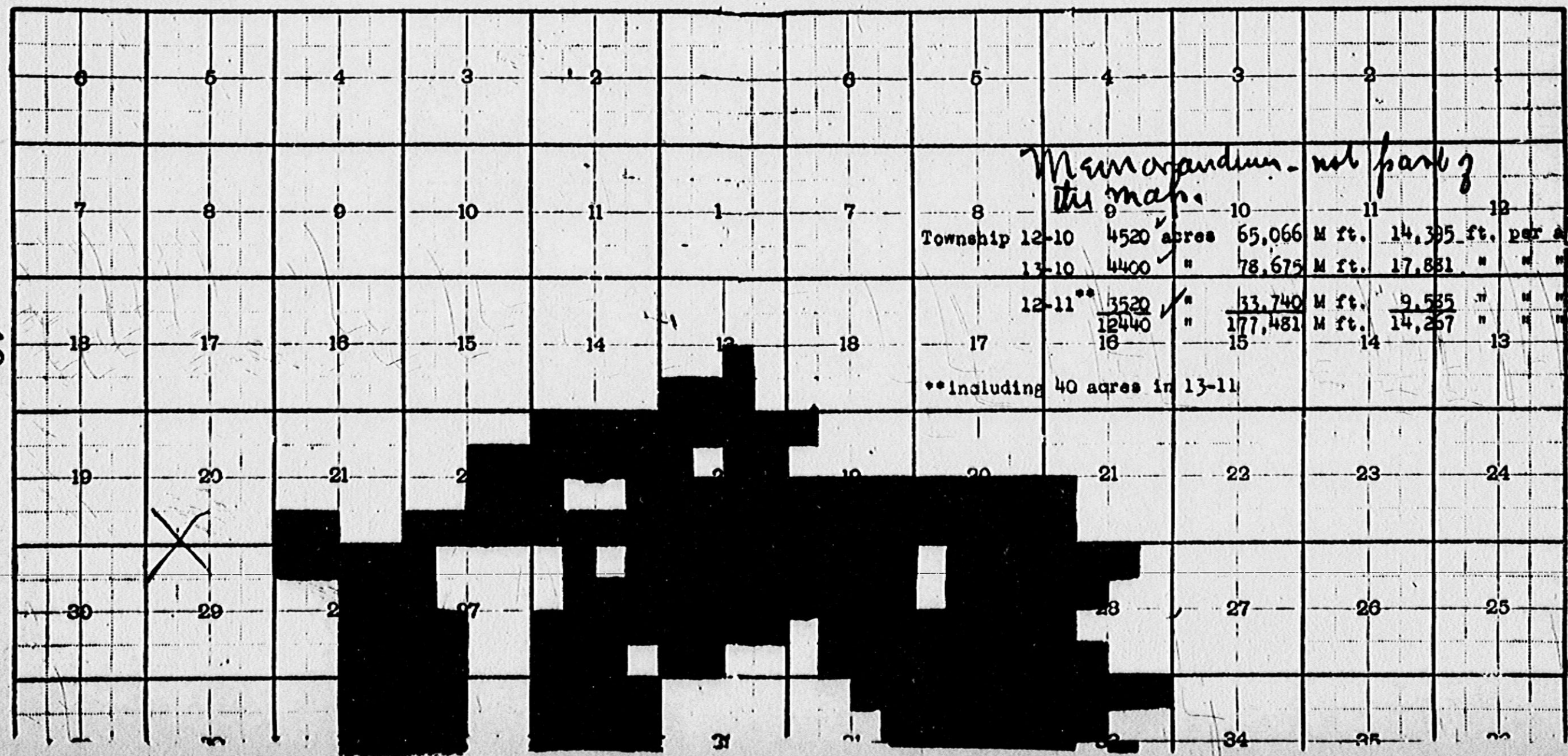
OF

Township No. 12 S Range No. 10 E

DIAGRAM

OF

Township No. 12 S Range No. 11 E



46

5858

Alworth-Washburn Co.
vs.
David Burnet Com. & c.

Interest paid on this note to May 1, 1927.

Interest on within note paid to MAY - 1 1928

Interest on within note paid to MAY 1 1929

Interest on within note paid to MAY 1 1930

The endorser hereof waives presentment for payment, protest, notice of protest and non-payment of this note.

ALWORTH-WASHBURN COMPANY

By J S Washburn President

and J Theis Tan Secretary.

U. S. BOARD OF TAX APPEALS
DIV. 8 DOCKET 45651
ADMITTED IN EVIDENCE
JUN 1 1 1931
PETITIONER'S
EXHIBIT 2
RESPONDENT'S

This note is one of a series of notes secured by contract of purchase of 22,440 acres of timber lands in Jefferson County, Oregon.

No. 17 Due May 1st, 1931 $26,000.00

On or before May first, 19 31, for value received, the Brooks-Scanlon Lumber Company, a corporation, promises to pay to the order of Alworth-Washburn Company, a corporation,

Twenty-Six Thousand - DOLLARS

at the Northern National Bank of Duluth, Minnesota, with interest at the rate of six per cent per annum until paid, interest payable annually.

BROOKS-SCANLON LUMBER COMPANY

by C. L. Brooks President

and F. E. Brooks Treasurer

PAID
FIRST NATIONAL BANK
MAY 1 1931
MINNEAPOLIS, MINN.
DISCOUNTS

79328 MAY 1 - 1931

The South Half (S. ½) of Section Twenty (20);

45 The West Half of the South West Quarter (W. ½ of S. W. ¼) of Section Twenty one (21);

The North West Quarter of the North East Quarter (N. W. ¼ of N. E. ¼), the entire North West Quarter (N. W. ¼), the West Half of the South West Quarter (W. ½ of S. W. ¼) and the South East Quarter of the South West Quarter (S. E. ¼ of S. W. ¼) of Section Twenty eight (28);

All of Section Twenty nine (29) except the West Half of the North West Quarter (W. ½ of N. W. ¼) thereof;

All of Section Thirty (30) except the West Half of the South West Quarter (W. ½ of S. W. ¼) thereof;

All of the East Half of Section Thirty one (31) except the South West Quarter of the North East Quarter (S. W. ¼ of N. E. ¼) of said section;

All of Section Thirty two (32);

The North Half of the North East Quarter (N. ½ of N. E. ¼), all of the North West Quarter (N. W. ¼), the West Half of the South West Quarter (W. ½ of S. W. ¼) and the North West Quarter of the South East Quarter (N. W. ¼ of S. E. ¼) of Section Thirty three (33).

Lands in Township Thirteen South of Range Eleven East.

The North West Quarter of the North West Quarter (N. W. ¼ of N. W. ¼) of Section Five (5).

Containing in all 12,440 Acres.

(Here follow side folios 46 and 47.)

48 U. S. Board of Tax Appeals, Division 8.

Docket 45651.

PETITIONER'S EXHIBIT 3.

Admitted in Evidence Jun. 14, 1931.

UNITED STATES OF AMERICA:

Treasury Department, Washington.

July 8, 1931.

Pursuant to the provisions of Section 661, Chapter 17, Title 28 of the United States Code (Section 882 of the Re-

vised Statutes of the United States), hereby certify that the annexed are true copies of the original and amended income tax returns, with attached schedules, filed on Form 1120 for the year 1926 by Alworth Washburn Company, 1600 Alworth Building, Duluth, Minnesota on file in this Department.

In witness whereof, I have hereunto set my hand, and caused the seal of the Treasury Department to be affixed, on the day and year first above written.

By direction of the Secretary of the Treasury:

[SEAL.] F. A. BIRGFELD,
F. A. BIRGFELD,
Chief Clerk, Treasury Department.

F. B. J. O. B. A. B. N. J. C. W.

(Here follow side folios 49, 50, 51, 52, 53, 54, 55, 56, 57 and 58.)

59 This amended return is filed to correct the taxpayer's original return for 1926.

The taxpayer has consistently kept its books of account on the basis of capitalizing carrying charges, such as interest, taxes, etc., during those years in which it was carrying its timber holdings without income from which to deduct them. Furthermore, has always prior to 1926 made its income tax returns consistent with that basis of accounting. Its return for 1926 was made originally without carrying charges only upon the findings of the Bureau that such carrying charges were not properly a part of timber cost.

Now comes Article 1561, Regulations 69, holding that the taxpayer may, through consistent practice, add to the cost (or other basis) of non-productive property carrying charges expended during non-productive years. This Article of Regulations 69 is based on a Law of practically identical wording with respect to the determination of profits from sale of property as the Laws of 1921 and 1924, and the taxpayer claims that it correctly interprets not only the Revenue Act of 1926 but the Acts of 1921 and 1924 as well, and must be given retroactive effect.

5858

Alworth-Washburn Co.
vs.
David Burnet Com. & c.

U. S. Internal Revenue
(Collector's Stamp)
CLOSED
OVERASSESSMENT
TAX $ See
INTEREST
PENALTY Amended
CLAIM NO.
DATE OF RAR
ADJUSTED BY
DIV SECT UNIT
DATE 1/14/28
EV'D. CC BY
DATE

CORPORATION INCOME TAX RETURN
For Calendar Year 1926

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1927

Page 1 of Return

File Code 19

Serial Number 401198

(Cashier's Stamp)

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

ALWORTH WASHBURN COMPANY (Name)

1600 ALWORTH BUILDING (Street and Number)

DULUTH MINNESOTA (Post office and State)

Paid U.S. Int. Rev. MAR 16 1927

MINNESOTA
Corded as above 81
Carded

Cash Check M. O. Cert. of Ind.
First Payment $ 6851.61

Date of Incorporation 1907

Under the Laws of what State or Country Minnesota

KIND OF BUSINESS Holding Company for Real Estate & Timber Investments IS THIS A CONSOLIDATED RETURN? No

Item and Instruction No.

GROSS INCOME

1. Gross Sales from Trading or Manufacturing, Less Returns and Allowances $ 476 758 70 — 754
2. Less Cost of Goods Sold:
   (a) Inventory at beginning of year
   (b) Merchandise bought for sale
   (c) Cost of manufacturing or otherwise producing goods (From Schedule A) 289 388 52
   (d) Total of lines (a), (b), and (c) $ 289 388 52
   (e) Less inventory at end of year 289 388 52
3. Gross Profit from Trading or Manufacturing (Item 1 minus Item 2) $ 187 370 18
4. Gross Profit from Operations Other Than Trading or Manufacturing. (State source of income):
   (a)
   (b)
   (c)
5. Interest on Bank Deposits, Notes, Mortgages, and Corporation Bonds 409 195
6. Rents
7. Royalties
8. Profit from Sale of Real Estate, Stocks, Bonds, and other Capital Assets (From Schedule B)
9. Dividends on Stock of Domestic Corporations
   Income (including dividends received on stock of foreign corporations). (State nature of income):
   (a)
   (b)
   (c)
11. Total Income in Items 3 to 10 $ 248 292 13

24 5 64

RECEIVED SEP 29 1928

RECEIVED AUG 18 1927 REVENUE AGENT ST. PAUL

DEDUCTIONS

12. Compensation of Officers (From Schedule C) 300 00
13. Rent on Business Property
14. Repairs (From Schedule D)
15. Interest 28 631 39
16. Taxes (From Schedule E) 48 798 83
17. Losses by Fire, Storm, etc. (From Schedule F)
18. Bad Debts (From Schedule G)
19. Dividends (From Schedule H)
20. Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule I)
21. Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see Instruction 21)
22. Other Deductions Not Reported Above. (Explain below, or on separate sheet):
   (a) Salaries and wages. (Not included in Item 2, 12, or 14 above)
   (b) Net Loss for prior year. (Submit schedule)
   (c) Schedule attached 11 470 41
   (d)
   (e)
   (f)
23. Total Deductions in Items 12 to 22 $ 45 281 63
24. Net Income (Item 11 minus Item 23) $ 203 010 50

RECEIVED WITH REMITTANCE Collector of Internal Revenue District of Minnesota MAR 15 1927 St. Paul Main Office

COMPUTATION OF TAX

25. Net Income (Item 24 above) $ 203 010 50
26. Less Credit of $2,000 (for a domestic corporation having a net income of less than $25,270)
27. Balance (Item 25 minus Item 26) $ 203 010 50
28. Income Tax (13½% of Item 27) $ 27 406 42
29. If the Net Income of a Domestic Corporation is Less Than $25,270, Enter the Amount in Excess of $25,000
30. Total Tax (Item 28 plus Item 29) $ 27 406 42
31. Less: Income Tax Paid at Source. (This credit can only be allowed to a nonresident foreign corporation) $
32. Income and Profits Taxes Paid to a Foreign Country or to a Possession of the United States by a domestic corporation
33. Balance of Tax (Item 30 minus Items 31 and 32) $ 27 406 42

An amended return must be marked "Amended" at top of return

Checks and drafts will be accepted only if payable to order of

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5858

Alworth-Washburn Co.
vs.
David Burnet Com. & c.

SCHEDULE A—COST OF MANUFACTURING OR PRODUCING GOODS (See Instructions 2)

Items	Amount	Items	Amount (Enter as Item 2c)
Salaries and wages	$		$
Material and supplies			

SCHEDULE B—PROFIT FROM SALE OF REAL ESTATE, STOCKS, BONDS, ETC. (See Instruction 8)

1. Kind of Property	2. Date Acquired	3. Amount Received	4. Depreciation Allowable Since Acquisition	5. Cost	6. Value as of March 1, 1913	7. Subsequent Improvements	8. Net Profit (Enter as Item 6)
		$	$	$	$	$	$

None

State how property was acquired

SCHEDULE C—COMPENSATION OF OFFICERS (See Instruction 12)

1. Name of Officer	2. Official Title	3. Time Devoted to Business	Shares of Stock Owned: 4. Common	Shares of Stock Owned: 5. Preferred	6. Amount of Compensation (Enter as Item 12)
Philip D. Gray	Sec-Treas	Part			$ 300.00

SCHEDULE D—COST OF REPAIRS (See Instruction 14)

1. Items	2. Amount (Enter as Item 14)
Salaries and wages	$

None

SCHEDULE E—TAXES PAID (See Instruction 16)

1. Items	2. Amount (Enter as Item 16)
Capital Stock Tax	$ 137.00
Real Estate	3508.10
Personal Property	73
	4879.83

SCHEDULE F—EXPLANATION OF LOSSES BY FIRE, STORM, ETC. (See Instruction 17)

1. Kind of Property	2. Date Acquired	3. Cost	4. Value as of March 1, 1913	5. Subsequent Improvements	6. Depreciation Allowable Since Acquisition	7. Insurance and Salvage Value	8. Net Loss (Enter as Item 17)
		$	$	$	$	$	$

None

State how property was acquired

SCHEDULE G—BAD DEBTS (See Instruction 18)

1. Year	2. Sales on Account	3. Bad Debts
1921	$	$
1922		
1923		
1924		
1925		

None

SCHEDULE H—DIVIDENDS DEDUCTIBLE (See Instruction 19)

1. Name of Corporation	Amount of Dividends: 2. Domestic	Amount of Dividends: 3. Foreign
	$	$

None

SCHEDULE I—EXPLANATION OF DEDUCTION FOR DEPRECIATION (See Instruction 20)

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquirement	5. Cost	6. Value as of March 1, 1913	Amount of Depreciation Charged Off: 7. Previous years	Amount of Depreciation Charged Off: 8. This year
				$	$	$	$

None

Attach a separate sheet if any of the above schedules do not provide sufficient space

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Alworth-Washburn Co.
vs.
David Burnet Com. & c.

Page 3 of Return

SCHEDULE K—BALANCE S[illegible] (See Instruction 43)

Items	Beginning of Taxable Year: Amount	Beginning of Taxable Year: Total	End of Taxable Year: Amount	End of Taxable Year: Total
ASSETS				
1. Cash		$ 1,686.69		$ 68,913.30
2. Notes receivable		None		None
3. Accounts receivable	$ None		$	
Less reserve for bad debts		None		None
4. Inventories:				
Raw materials	$		$	
Work in process				
Finished goods				
Supplies				
		None		None
5. Investments:				
Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	$		$	
Securities issued under the Federal Farm Loan Act, or under such Act as amended				
Obligations of the United States or its possessions		None		None
6. Loans (describe fully):				
Installment Notes Receivable	$ 375,640.68		$ 467,720.00	
		375,640.68		467,720.00
7. Deferred charges:				
Prepaid insurance	$		$	
Prepaid taxes		None		None
8. Capital assets:				
Land		39,927.99		51,348.26
Buildings	$		$	
Machinery and equipment				
Furniture and fixtures				
Delivery equipment				
Cost of Installment Sales	237,416.41		287,237.40	
	$ 237,416.41		$ 287,237.40	
Less reserves for depreciation and depletion		237,416.41		287,237
9. Patents		None		None
10. Good will		None		None
11. Other assets (describe fully):				
Liquidating Dividends	$ 166,298.33		$ 302,741.99	
		166,298.33		302,741.99
12. Total Assets		$ 1,171,969.88		$ 1,116,308.95 ✓
LIABILITIES				
13. Notes payable		$ None		$ None
14. Accounts payable		4,320.60		None
15. Accrued expenses (describe fully):				
	$		$	
		None		None
16. Other liabilities (describe fully):				
Appreciation Surplus	$ 274,134.79		$ 121,182.58	
Installment Sales (Contr.)	375,640.68 +		467,720.00	
		649,775.47 ✓		588,902.53 ✓
17. Capital stock:				
Preferred stock (less stock in treasury)	$ —		$ —	
Common stock (less stock in treasury)	500,000.00	500,000.00	500,000.00	500,000.00 ✓
18. Surplus	$ 178,744.41		$ 27,406.42	
19. Undivided profits		178,744.41 ✓		27,406.42 ✓
20. Total Liabilities		$ 1,171,969.88 ✓		$ 1,116,308.95 ✓

Remarks

8—16687

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Alworth-Washburn Co.
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David Burnet Com. & c.

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SCHEDULE L—RECONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

1. Net income from Item 24, page 1 of the return	$203	010	50
2. Nontaxable income:			
(a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia		—	
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended		—	
(c) Interest on obligations of the United States or its possessions		—	
(d) Dividends deductible under Section 234(a) 6 of the Revenue Act of 1926		—	
(e) Proceeds of life insurance policies paid upon the death of the insured		—	
(f) Other items of nontaxable income (to be detailed):			
(1)		—	
(2)		—	
(3)		—	
3. Charges against reserve for bad debts, if Item 18, page 1 of return, is not an addition to a reserve		—	
4. Charges against reserves for contingencies, etc. (to be detailed):			
(a)		—	
(b)		—	
(c)		—	
5. Total of Lines 1 to 4, inclusive	$203	010	50
6. Total from Line 14		—	
7. Net profit for year as shown by books, before any adjustments are made therein (Line 5 minus Line 6)	$203	010	50
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year	17	874	41
9. Other credits to surplus (to be detailed):			
(a)		—	
(b)		—	
(c)		—	
10. Total of Lines 7 to 9, inclusive	$220	884	91
11. Total from Line 17	193	478	49
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)	$27	406	42

13. Unallowable deductions:			
(a) Donations, gratuities, and contributions	$	—	
(b) Income and profits taxes paid to the United States, and so much of such taxes paid to its possessions or foreign countries as are claimed as a credit in Item 32, page 1 of the return		—	
(c) Federal taxes paid on tax-free covenant bonds		—	
(d) Special improvement taxes tending to increase the value of the property assessed		—	
(e) Furniture and fixtures, additions, or betterments treated as expenses on the books		—	
(f) Replacements and renewals		—	
(g) Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary		—	
(h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation		—	
(i) Additions to reserve for bad debts which are not included in Item 18, page 1 of return		—	
(j) Additions to reserves for contingencies, etc. (to be detailed):			
(1)		—	
(2)		—	
(3)		—	
(k) Other unallowable deductions (to be detailed):			
(1)		—	
(2)		—	
(3)		—	
14. Total of Line 13	$	—	
15. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property):			
(a) Date paid .... Character Cash	$175	604	08
(b) Date paid .... Character		—	
(c) Date paid .... Character		—	
(d) Date paid .... Character		—	
16. Other debits to surplus (to be detailed):			
(a) Income Tax 1925	17	874	41
(b)		—	
(c)		—	
17. Total of Lines 15 and 16	$193	478	49

QUESTIONS

KIND OF BUSINESS

1. By means of the key letters given below, identify the corporation's main income-producing activity with one of the general classes, and follow this by a special description of the business sufficient to give the information called for under each general class.

A.—Agriculture and related industries, including fishing, logging, ice harvesting, etc., and also the leasing of such property. State the product or products. B.—Mining and quarrying, including gas and oil wells, and also the leasing of such property. State the product or products. C.—Manufacturing. State the product and also the material if not implied by the name of the product. D.—Construction—excavations, buildings, bridges, railroads, ships, etc., also equipping and installing same with systems, devices, or machinery, without their manufacture. State nature of structures built, materials used, or kind of installations. E1.—Transportation—rail, water, local, etc. State the kind and special product transported, if any. E2.—Public utilities—gas (natural, coal, or water); electric light or power (hydro or steam generated); heating (steam or hot water); telephone; waterworks or power. E3.—Storage—without trading or profit from sales—(elevators, warehouses, stockyards, etc.). State product stored. E4.—Leasing transportation or utilities. State kind of property. F.—Trading in goods bought and not produced by the trading concern. State manner of trade, whether wholesale, retail, or commission, and product handled. Sales with storage with profit primarily from sales. G.—Service—domestic, including hotels, restaurants, etc.; amusements; other professional, personal, or technical service. State the service. H.—Finance, including banking, real estate, insurance. I.—Concerns not falling in above classes (a) because of combining several of them with no predominant business, or (b) for other reasons.

2. Concerns whose business involves activity falling in two or more of the above general classes, where the *same product* is concerned, should report business as identified with but one of the above general classes; for example, concerns in A or B which also transport and market their own product exclusively or mainly, should still be identified with classes A or B; concerns in C (manufacturing) which own or control their source of material supply in A or B and which also transport, sell, or install their own product exclusively or mainly, should be identified with manufacturing; concerns in D may control or own the source of supply of materials used exclusively or mainly in their constructive work; concerns in E1 or E2 may own or control the source of their material or power; concerns in F may transport or store their own merchandise, but its production would identify them with A, B, or C.

3. Answers:
(a) General class (use key letter designation) I
(b) Main income-producing business (give specifically the information called for under each key letter, also whether acting as principal, or as agent on commission; state if inactive or in liquidation) Holding Company for Lumber Investments

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTION 38

4. Does the corporation own 95 per cent or more of the outstanding capital stock of another domestic corporation or of other corporations? No

5. Is over 95 per cent or more of your outstanding capital stock owned by another corporation? No

6. Is 95 per cent or more of your outstanding capital stock as well as 95 per cent or more of the outstanding capital stock of another corporation or of other corporations owned or controlled by the same individual or partnership or by the same individuals, partnerships, or corporations in substantially the same proportion? No

7. If the answer to questions 4, 5, and 6, or to any of them, is "yes," answer the following:

(a) Did the corporation file Forms 851, 852, 853, and 853A for the taxable year 1922 or subsequent taxable years? — If the answer to this question is "yes," these forms will not be required, except under the circumstances described in question (b). If the answer to this question is "no," and the answer to questions 4, 5, and 6, or to any of them, is "yes," procure from the Collector of Internal Revenue for your district Forms 851, 852, 853, and 853A, Affiliations Schedules 1, 2, 3, and 4, which shall be filled in and filed as a part of this return. If the answer to this question is "no," question (b) need not be answered.

(b) Did substantially the same conditions, as are set out in the Affiliations Schedules filed for 1925 or prior years, obtain during the entire taxable year 1926? Yes If the answer to this question is "no," a statement, setting forth the particulars in which the situation has changed, should be attached to and made a part of this return. If there have been substantial changes in stockholdings, a complete schedule of such changes should be submitted on Form 853, Affiliations Schedule 3. If there are companies other than those covered by the Affiliations Schedules for prior years which, applying the tests contained in questions 4, 5, or 6, may have come into the affiliated group since 1925, Forms 851, 852, 853, and 853A, are required for the entire group for the taxable year.

(c) Did the corporation file a consolidated return for the preceding taxable year? No

PREDECESSOR BUSINESS

8. Did the corporation file a return under the same name for the preceding taxable year? Yes If not, was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or the preceding taxable year? — If answer is "yes," give name and address of each predecessor business.

BASIS OF RETURN

9. Is this return made on the basis of actual receipts and disbursements? Yes If not, describe fully what other basis or method was used in computing net income.

LIST OF ATTACHED SCHEDULES

10. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the taxpayer should be placed on each separate schedule accompanying the return.

22 (c) Deductions
Computation of Gross Profit

AFFIDAVIT

We, the undersigned, president and treasurer of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return made in good faith, for the taxable year as stated, pursuant to the Revenue Act of 1926 and the Regulations issued under authority thereof.

Sworn to and subscribed before me this 4th day of March, 1927

NOTARIAL SEAL

Lola M. Bordeleau
(Signature of officer administering oath)

(Title)

CORPORATE SEAL

[signature] President.

Philip W. Ray Treasurer.
Sec'y

LOLA M. BORDELEAU
Notary Public, St. Louis Co., Minn.
My Commission Expires January 8, 1934

GOVERNMENT PRINTING OFFICE 9—1487

Alworth-Washburn Co.
vs.
David Burnet Com. & c.

3-1

ALWORTH-WASHBURN COMPANY

Schedule 22 (c)

Deductions

Annual License	200.00
Abstract Charges	142.80
Accounting	486.94
Telegrams	5.15
Indemnity Insurance	10.00
Express	.93
Exchange	2.70
Printing	4.75
Commissions Paid	10,617.14
	$11,470.41

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Alworth-Washburn Co.
vs.
David Burnet Com. & c.

3-2

ALWORTH-WASHBURN COMPANY

STATEMENT SHOWING COMPUTATION OF GROSS PROFIT

Reference IT:CA:2554-12

INSTALLMENT SALES OF LAND AND TIMBER

1923 Southern Group :

Item	Fair Value	Sale Price
Land 24,280 A.	$ 23,180.00	
Timber 334,368-M- Ft.	658,373.48	$1,189,101.67
Additional Purchases in 1923	13,650.00	
	$695,203.48	$1,189,101.67
1926 Receipts (final installment)		$ 375,640.68
Cost 31.5903% of $695,203.48		219,616.86
Gross Profit		$ 156,023.82

1926 - Northern Group :

Item	Fair Value	Sale Price
Land 12,440 A.	$ 12,440.00	
Timber, 177,651 M ft.	326,769.51	$ 588,838.02
	$339,209.51	$ 588,838.02
1926 Receipts		$ 121,118.02
Cost 20.5689% of $339,209.51		69,771.66
Gross Profit		$ 51,346.36

1926 Gross Profit, Southern Group -	$ 156,023.82
1926 " " , Northern Group -	51,346.36
Total 1926 Gross Profit	$ 207,370.18

5858

Alworth-Washburn Co.
vs.
David Burnet Com. & C.

U. S. INTERNAL REVENUE
(Auditor's Stamp)

CLOSED
OVERASSESSMENT
TAX $1,070.27
INTEREST
PENALTY
CLAIM NO. 103796
DATE OF RAR 2-13-28
ADJUSTED BY Williamson
DIV. C SEC. Rebate
DATE 4-17-28
CC OK
DATE

CORPORATION INCOME TAX RETURN
For Calendar Year 1926

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1927

Page 1 of Return 55

File Code 19

Serial Number Minn
(Cashier's Stamp)
1120

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

ALWORTH - WASHBURN COMPANY
(Name)
1600 ALWORTH BUILDING
(Street and Number)
DULUTH, MINNESOTA
(Post office and State)

Cash, Check M.O. Cert. of Ind.
First Payment
$
Carried
As

Date of Incorporation 1907

Under the Laws of what State or Country Minnesota

KIND OF BUSINESS Holding Company for Real Estate and Timber Investments IS THIS A CONSOLIDATED RETURN? No

Item and Instruction No.										
	GROSS INCOME									
1.	Gross Sales from Trading or Manufacturing, Less Returns and Allowances				$	496	758	70		
2.	Less Cost of Goods Sold:									
	(a) Inventory at beginning of year	$								
	(b) Merchandise bought for sale									
	(c) Cost of manufacturing or otherwise producing goods (From Schedule A)		319	246	12					
	(d) Total of lines (a), (b), and (c)	$	319	246	12					
	(e) Less inventory at end of year					319	246	12		
3.	Gross Profit from Trading or Manufacturing (Item 1 minus Item 2)				$	177	512	58		
4.	Gross Profit from Operations Other Than Trading or Manufacturing. (State source of income):									
	(a)									
	(b)									
	(c)									
5.	Interest on Bank Deposits, Notes, Mortgages, and Corporation Bonds					40	921	95		
6.	Rents									
7.	Royalties									
8.	Profit from Sale of Real Estate, Stocks, Bonds, and other Capital Assets (From Schedule B)									
9.	Dividends on Stock of Domestic Corporations									
10.	Other Income (including dividends received on stock of foreign corporations). (State nature of income):									
	(a)									
	(b)									
	(c)									
11.	TOTAL INCOME IN ITEMS 3 TO 10								$ 218	434 53
	DEDUCTIONS									
12.	Compensation of Officers (From Schedule C)				$		300	00		
13.	Rent on Business Property									
14.	Repairs (From Schedule D)									
15.	Interest					28	131	39		
16.	Taxes (From Schedule E)					4	879	83		
17.	Losses by Fire, Storm, etc. (From Schedule F)									
18.	Bad Debts (From Schedule G)									
19.	Dividends (From Schedule H)									
20.	Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule I)									
21.	Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see Instruction 21)									
22.	Other Deductions Not Reported Above. (Explain below, or on separate sheet):									
	(a) Salaries and wages. (Not included in Item 2, 12, or 14 above)									
	(b) Net Loss for prior year. (Submit schedule)									
	(c) Schedule Attached					11	470	41		
	(d)									
	(e)									
	(f)									
23.	TOTAL DEDUCTIONS IN ITEMS 12 TO 22								$ 45	281 63
24	NET INCOME (Item 11 minus Item 23)								$ 173	152 90

COMPUTATION OF TAX

25. Net Income (Item 24 above)	$	173	152	90	28. Income Tax (13½% of Item 27)	$	23	375	64
26. Less Credit of $2,000 (for a domestic corporation having a net income of less than $25,270)					29. If the Net Income of a Domestic Corporation is Less Than $25,270, Enter the Amount in Excess of $25,000				
27. Balance (Item 25 minus Item 26)	$	173	152	90	30. Total Tax (Item 28 plus Item 29)	$	23	375	64
31. Less: Income Tax Paid at Source. (This credit can only be allowed to a nonresident foreign corporation)									
32. Income and Profits Taxes Paid to a Foreign Country or to a Possession of the United States by a domestic corporation									
33. Balance of Tax (Item 30 minus Items 31 and 32)						$	23	375	64

An amended return must be marked "Amended" at top of return

Checks and drafts will be accepted only if payable at par at least

Tax paid 27,406.42

Original 451198
1927 List

Refund due 4,030.78

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5858

Alworth-Washburn Co.
vs.
David Burnet Com. & c.

Items	Amount	Items	Amount (Enter as Item 2c)
Salaries and wages	$		$
Material and supplies			

SCHEDULE B—PROFIT FROM SALE OF REAL ESTATE, STOCKS, BONDS, ETC. (See Instruction 8)

1. Kind of Property	2. Date Acquired	3. Amount Received	4. Depreciation Allowable Since Acquisition	5. Cost	6. Value as of March 1, 1913	7. Subsequent Improvements	8. Net Profit (Enter as Item 5)
		$	$	$	$	$	$
							None

State how property was acquired

SCHEDULE C—COMPENSATION OF OFFICERS (See Instruction 12)

1. Name of Officer	2. Official Title	3. Time Devoted to Business	Shares of Stock Owned: 4. Common	Shares of Stock Owned: 5. Preferred	6. Amount of Compensation (Enter as Item 12)
Philip L Ray	Sec Treas	Part	11		$ 300 00

SCHEDULE D—COST OF REPAIRS (See Instruction 14)

1. Items	2. Amount (Enter as Item 14)
Salaries and wages	$

SCHEDULE E—TAXES PAID (See Instruction 16)

1. Items	2. Amount (Enter as Item 16)
Capital Stock Tax	$ 1,371 00
Real Estate	3,508 10
Personal Property	73
	4,879 83

SCHEDULE F—EXPLANATION OF LOSSES BY FIRE, STORM, ETC. (See Instruction 17)

1. Kind of Property	2. Date Acquired	3. Cost	4. Value as of March 1, 1913	5. Subsequent Improvements	6. Depreciation Allowable Since Acquisition	7. Insurance and Salvage Value	8. Net Loss (Enter as Item 17)
		$	$	$	$	$	$
							None

State how property was acquired

SCHEDULE G—BAD DEBTS (See Instruction 18)

1. Year	2. Sales on Account	3. Bad Debts
1921	$	$
1922		
1923		
1924		
1925		None

SCHEDULE H—DIVIDENDS DEDUCTIBLE (See Instruction 19)

1. Name of Corporation	Amount of Dividends: 2. Domestic	Amount of Dividends: 3. Foreign
	$	$
		None

SCHEDULE I—EXPLANATION OF DEDUCTION FOR DEPRECIATION (See Instruction 20)

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquirement	5. Cost	6. Value as of March 1, 1913	Amount of Depreciation Charged Off: 7. Previous years	Amount of Depreciation Charged Off: 8. This year
				$	$	$	$
							None

Attach a separate sheet if any of the above schedules do not provide sufficient space

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BALANCE SHEETS (See Instruction 15)

Items	Beginning of Taxable Year: Amount	Beginning of Taxable Year: Total	End of Taxable Year: Amount	End of Taxable Year: Total
ASSETS				
1. Cash		$ 168469		$ 689130
2. Notes receivable				
3. Accounts receivable	$		$	
Less reserve for bad debts				
4. Inventories:				
Raw materials	$		$	
Work in process				
Finished goods				
Supplies				
5. Investments:				
Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	$		$	
Securities issued under the Federal Farm Loan Act, or under such Act as amended				
Obligations of the United States or its possessions				
6. Loans (describe fully):				
Installment Notes Receivable	$ 375640 68		$ 467720 00	
		375640 68		467720 00
7. Deferred charges:				
Prepaid insurance	$		$	
Prepaid taxes				
8. Capital assets:				
Land and Timber		377751 23		
Buildings	$		$	
Machinery and equipment				
Furniture and fixtures				
Delivery equipment				
Unit of Installment Sales	241546 47		300051 58	
	$ 241546 47		$ 300051 58	
Less reserves for depreciation and depletion		241546 47		300051 58
9. Patents				
10. Good will				
11. Other assets (describe fully):				
Liquidating Dividends	$ 199331 82		$ 365598 12	
		199331 82		365598 12
12. Total Assets		$ 1195956 89		$ 1140261 00
LIABILITIES				
13. Notes payable		$		$
14. Accounts payable		4320 00		
15. Accrued expenses (describe fully):				
	$		$	
16. Other liabilities (describe fully):				
Depreciation Surplus	$ 298121 80		$ 145134 58	
Installment sales (contra)	375640 68		467720 00	
		673762 48		612854 58
17. Capital stock:				
Preferred stock (less stock in treasury)	$		$	
Common stock (less stock in treasury)	500000 00	500000 00	500000 00	500000 00
18. Surplus	$ 17874 41		$ 27406 42	
19. Undivided profits		17874 41		27406 42
20. Total Liabilities		$ 1195956 89		$ 1140261 00

Remarks

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SCHEDULE L—RECONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

Item	$		
1. Net income from Item 24, page 1 of the return	173	152	90
2. Nontaxable income:			
(a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia			
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended			
(c) Interest on obligations of the United States or its possessions			
(d) Dividends deductible under Section 234(a) 6 of the Revenue Act of 1926			
(e) Proceeds of life insurance policies paid upon the death of the insured			
(f) Other items of nontaxable income (to be detailed):			
(1)			
(2)			
(3)			
3. Charges against reserve for bad debts, if Item 18, page 1 of return, is not an addition to a reserve			
4. Charges against reserves for contingencies, etc. (to be detailed):			
(a)			
(b)			
(c)			
5. Total of Lines 1 to 4, inclusive	173	152	90
6. Total from Line 14			
7. Net profit for year as shown by books, before any adjustments are made therein (Line 5 minus Line 6)	173	152	90
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year	17	874	41
9. Other credits to surplus (to be detailed):			
(a)			
(b)			
(c)			
10. Total of Lines 7 to 9, inclusive	191	027	31
11. Total from Line 17	163	620	89
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)	27	406	42

Item	$		
13. Unallowable deductions:			
(a) Donations, gratuities, and contributions			
(b) Income and profits taxes paid to the United States, and so much of such taxes paid to its possessions or foreign countries as are claimed as a credit in Item 32, page 1 of the return			
(c) Federal taxes paid on tax-free covenant bonds			
(d) Special improvement taxes tending to increase the value of the property assessed			
(e) Furniture and fixtures, additions, or betterments treated as expense on the books			
(f) Replacements and renewals			
(g) Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary			
(h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation			
(i) Additions to reserve for bad debts which are not included in Item 18, page 1 of return			
(j) Additions to reserves for contingencies, etc. (to be detailed):			
(1)			
(2)			
(3)			
(k) Other unallowable deductions (to be detailed):			
(1)			
(2)			
(3)			
14. Total of Line 13			
15. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property):			
(a) Date paid .... Character *cash*	145	746	48
(b) Date paid .... Character			
(c) Date paid .... Character			
(d) Date paid .... Character			
16. Other debits to surplus (to be detailed):			
(a) *Income tax 1925*	17	874	41
(b)			
(c)			
17. Total of Lines 15 and 16	163	620	89

QUESTIONS

KIND OF BUSINESS

1. By means of the key letters given below, identify the corporation's main income-producing activity with one of the general classes, and follow this by a special description of the business sufficient to give the information called for under each general class.

A.—Agriculture and related industries, including fishing, logging, ice harvesting, etc., and also the leasing of such property. State the product or products. B.—Mining and quarrying, including gas and oil wells, and also the leasing of such property. State the product or products. C.—Manufacturing. State the product and also the material if not implied by the name of the product. D.—Construction—excavations, buildings, bridges, railroads, ships, etc., also equipping and installing same with systems, devices, or machinery, without their manufacture. State nature of structures built, materials used, or kind of installations. E1.—Transportation—rail, water, local, etc. State the kind and special product transported, if any. E2.—Public utilities—gas (natural, coal, or water); electric light or power (hydro or steam generated); heating (steam or hot water); telephone; waterworks or power. E3.—Storage—without trading or profit from sales—(elevators, warehouses, stockyards, etc.). State product stored. E4.—Leasing transportation or utilities. State kind of property. F.—Trading in goods bought and not produced by the trading concern. State manner of trade, whether wholesale, retail, or commission, and product handled. Sales with storage with profit primarily from sales. G.—Service—domestic, including hotels, restaurants, etc.; amusements; other professional, personal, or technical service. State the service. H.—Finance, including banking, real estate, insurance. I.—Concerns not falling in above classes (a) because of combining several of them with no predominant business, or (b) for other reasons.

2. Concerns whose business involves activity falling in two or more of the above general classes, where the *same product* is concerned, should report business as identified with but one of the above general classes; for example, concerns in A or B which also transport and market their own product exclusively or mainly, should still be identified with classes A or B; concerns in C (manufacturing) which own or control their source of material supply in A or B and which also transport, sell, or install their own product exclusively or mainly, should be identified with manufacturing; concerns in D may control or own the source of supply of materials used exclusively or mainly in their constructive work; concerns in E1 or E2 may own or control the source of their material or power; concerns in F may transport or store their own merchandise, but its production would identify them with A, B, or C.

3. Answers:
(a) General class (use key letter designation) *I*
(b) Main income-producing business (give specifically the information called for under each key letter, also whether acting as principal, or as agent on commission; state if inactive or in liquidation):
Holding company for Timber Investments

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTION 2?

4. Does the corporation own 95 per cent or more of the outstanding capital stock of another domestic corporation or of other corporations? *No*

5. Is over 95 per cent or more of your outstanding capital stock owned by another corporation? *No*

6. Is 95 per cent or more of your outstanding capital stock as well as 95 per cent or more of the outstanding capital stock of another corporation or of other corporations owned or controlled by the same individual or partnership or by the same individuals, partnerships, or corporations in substantially the same proportion? *No*

7. If the answer to questions 4, 5, and 6, or to any of them, is "yes," answer the following:

(a) Did the corporation file Forms 851, 852, 853, and 853A for the taxable year 1922 or subsequent taxable years? *✓* If the answer to this question is "yes," these forms will not be required, except under the circumstances described in question (b). If the answer to this question is "no," and the answer to questions 4, 5, and 6, or to any of them, is "yes," procure from the Collector of Internal Revenue for your district Forms 851, 852, 853, and 853A, Affiliations Schedules 1, 2, 3, and 4, which shall be filled in and filed as a part of this return. If the answer to this question is "no," question (b) need not be answered.

(b) Did substantially the same conditions, as are set out in the Affiliations Schedules filed for 1925 or prior years, obtain during the entire taxable year 1926? *Yes* If the answer to this question is "no," a statement, setting forth the particulars in which the situation has changed, should be attached to and made a part of this return. If there have been substantial changes in stockholdings, a complete schedule of such changes should be submitted on Form 853, Affiliations Schedule 3. If there are companies other than those covered by the Affiliations Schedules for prior years which, applying the tests contained in questions 4, 5, or 6, may have come into the affiliated group since 1925, Forms 851, 852, 853, and 853A, are required for the entire group for the taxable year.

(c) Did the corporation file a consolidated return for the preceding taxable year? *No*

PREDECESSOR BUSINESS

8. Did the corporation file a return under the same name for the preceding taxable year? *Yes* If not, was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or the preceding taxable year? *✓* If answer is "yes," give name and address of each predecessor business.
✓

BASIS OF RETURN

9. Is this return made on the basis of actual receipts and disbursements? *Yes* If not, describe fully what other basis or method was used in computing net income.
✓

LIST OF ATTACHED SCHEDULES

10. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the taxpayer should be placed on each separate schedule accompanying the return.

Schedule A - Computation of Cost of Land and Timber Sold
" 22(c) - Deductions

AFFIDAVIT

We, the undersigned, president and treasurer of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return made in good faith, for the taxable year as stated, pursuant to the Revenue Act of 1926 and the Regulations issued under authority thereof.

Sworn to and subscribed before me this *16th* day of *February*, 192*8*

NOTARIAL SEAL

A. J. Nolan (Signature of officer administering oath)

Notary Public (Title)

A. J. NOLAN
Notary Public, St. Louis Co., Minn
My Commission expires [illegible]

J. A. Washburn President.

CORPORATE SEAL

Phillip W. Ray ~~Treasurer.~~ *Secy*

60 Alworth Washburn Company.

Cost of Land Sold (Schedule A).

Southern Group:		
Fair Value — Govt. Statement IT:CA:2554-12	$695,203.48	
Carrying charges 3-1-13 to 12-31-22 (prorated)	69,419.21	
Total	$764,622.69	
Total sales price $1,189,101.67; $375,640.68 collected in 1926 is 31.5902%; 31.5902% of cost, $764,622.69		$241,546.47
Northern Group:		
Fair Value — Govt. Statement IT:CA:2554-12	$339,209.51	
Carrying charges 3-1-13 to 12-31-22 (prorated)	38,541.72	
Total Cost	$377,751.23	
Total Sales prices $588,838.02; $100,000.00 collected in 1926 is 20.569%; 20.569% of Cost, $377,751.23		77,699.65
Total Cost of Land Sold		$319,246.12

61 Alworth Washburn Company.

Schedule 22 (C), Deductions.

Annual License	$200.00
Abstract Charges	142.80
Accounting	486.94
Telegrams	5.15
Indemnity Insurance	10.00
Express	.93
Exchange	2.70
Printing	4.75
Commissions Paid	10,617.14
	$11,470.41

62 U. S. Board of Tax Appeals, Div. 8.

Docket 45651.

PETITIONER'S EXHIBIT 4.

Admitted in Evidence Jun. 14, 1931.

UNITED STATES OF AMERICA:

Treasury Department, Washington.

July 8, 1931.

Pursuant to the provisions of Section 661, Chapter 17, Title 28 of the United States Code (Section 882 of the Revised Statutes of the United States), hereby certify that the annexed is a true copy of the income tax return filed on Form 1120 for the year 1928 by Alworth Washburn Company, 1600 Alworth Building, Duluth, Minnesota.

On file in this Department.

In witness whereof, I have hereunto set my hand, and caused the seal of the Treasury Department to be affixed, on the day and year first above written.

By direction of the Secretary of the Treasury:

[SEAL.] F. A. BIRGFELD,

F. A. BIRGFELD,

Chief Clerk, Treasury Department.

F. B. J. O. B. A. B. N. J. C. W.

(Here follow side folios 63, 64, 65, 66, 67, 68, 69, 70, 71, 72, 73, 74, 75, 76, 77, 78, 79, 80, and 81.)

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Page 1 of Return

For Calendar Year 1928

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1929

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

ALWORTH WASHBURN COMPANY (Name)
1600 ALWORTH BUILDING (Street and number)
DULUTH MINNESOTA (Post office and State)

File Code 19
Serial Number 401187

(Cashier's Stamp) MAR 16 1929

Cash Check M.O. Cert. of Ind.
First Payment
$ 974.65
Carded
As

Date of Incorporation 1907

Under the Laws of what State or Country Minnesota

Kind of Business Holding Company for Real Estate and Timber Investments. Is This a Consolidated Return of Two or More Corporations? No

24
0
8
89

GROSS INCOME

Item	Amount
1. Gross Sales from Trading or Manufacturing, Less Returns and Allowances	$ 98,180.00
2. Less Cost of Goods Sold:	
(a) Inventory at close of preceding year	$
(b) Merchandise bought for sale	
(c) Cost of manufacturing or otherwise producing goods (From Schedule A)	62,984.35
(d) Total of lines (a), (b), and (c)	$ 62,984.35
(e) Less inventory at end of year	62,984.35
3. Gross Profit from Trading or Manufacturing (Item 1 minus Item 2)	$ 35,195.65
4. Gross Profit from Operations Other Than Trading or Manufacturing. (State source of income):	
(a)	
(b)	
(c)	
5. Interest on Bank Deposits, Notes, Mortgages, and Corporation Bonds	166.49
6. Rents	
7. Royalties	
8. Profit from Sale of Real Estate, Stocks, Bonds, and other Capital Assets (From Schedule B)	
9. Dividends on Stock of Domestic Corporations	
10. Other Income (including dividends received on stock of foreign corporations) (State nature of income):	
(a)	
(b)	
(c)	
11. TOTAL INCOME IN ITEMS 3 TO 10	$ 35,962.14

RECEIVED
JUL 3 1929
INTERNAL REVENUE AGENT IN CHARGE, MINNESOTA.

RECEIVED WITH REMIT COLLECTOR'S OFFICE MAR 16 1929

DEDUCTIONS

Item	Amount
12. Compensation of Officers (From Schedule C)	$ 150.00
13. Rent on Business Property	
14. Repairs (From Schedule D)	
15. Interest	
16. Taxes (From Schedule E)	1427.40
17. Losses (From Schedule F)	
18. Bad Debts (From Schedule G)	
19. Dividends (From Schedule H)	
20. Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule I)	
21. Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see Instruction 21)	
22. Other Deductions Not Reported Above. (Explain below, or on separate sheet):	
(a) Salaries and wages. (Not included in Item 2, 12, or 14 above)	
(b) Net Loss for prior year. (Submit schedule)	
(c) Auditing	1002.12
(d) Fees and Licenses	210.00
(e) Telephone and Telegraph	34.68
(f)	
23. TOTAL DEDUCTIONS IN ITEMS 12 TO 22	$ 2,874.00
24. NET INCOME (Item 11 minus Item 23)	$ 32,488.14

COMPUTATION OF TAX

Item	Amount
25. Net Income (Item 24 above)	$ 32,488.14
26. Less Credit of $3,000 (for a domestic corporation having a net income of less than $25,000)	
27. Balance (Item 25 minus Item 26)	$ 32,488.14
28. Income Tax (12% of Item 27)	$ 3,898.58
29. If the Net Income of a Domestic Corporation is less than $25,000, enter the amount in excess of $25,000	
30. Total Tax (Item 28 plus Item 29)	$ 3,898.58
31. Less: Income Tax Paid at Source. (This credit can only be allowed to a nonresident foreign corporation)	$
32. Income and Profits Taxes Paid to a Foreign Country or United States possession by a domestic corporation (see Inst. 27)	
33. Balance of Tax (Item 30 minus Items 31 and 32)	$ [illegible]

An amended return must be marked "Amended" at top of return

Checks and drafts will be accepted only if payable at par

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SCHEDULE A—COST OF MANUFACTURING OR PRODUCING GOODS (See Instruction 2)

Items	Amount	Its	Amount (Enter as Item 9a)
Salaries and wages	$	Total Sales price $558,538.02	$
Material and supplies		$98,180.00 collected in 1928 is	
		16.6735 %	
		16.6735 % of Total Cost, $377,751.23	62,984.35

SCHEDULE B—PROFIT FROM SALE OF REAL ESTATE, STOCKS, BONDS, ETC. (See Instruction 8)

1. Kind of Property	2. Date Acquired	3. Amount Received	4. Depreciation Allowable Since Acquisition	5. Cost	6. Value as of March 1, 1913	7. Subsequent Improvements	8. Net Profit (Enter as Item 6)
		$	$	$	$	$	$

State how property was acquired

SCHEDULE C—COMPENSATION OF OFFICERS (See Instruction 12)

1. Name of Officer	2. Official Title	3. Time Devoted to Business	Shares of Stock Owned: 4. Common	Shares of Stock Owned: 5. Preferred	6. Amount of Compensation (Enter as Item 12)
Philip L. Rage	Sec-Treas.	Part			$ 150.00

SCHEDULE D—COST OF REPAIRS (See Instruction 14)

1. Items	2. Amount (Enter as Item 14)
Salaries and wages	$

SCHEDULE E—TAXES PAID (See Instruction 16)

1. Items	2. Amount (Enter as Item 16)
Personal Property Money and Credits	$ 1477.20

SCHEDULE F—EXPLANATION OF LOSSES BY FIRE, STORM, ETC. (See Instruction 17)

1. Kind of Property	2. Date Acquired	3. Cost	4. Value as of March 1, 1913	5. Subsequent Improvements	6. Depreciation Allowable Since Acquisition	7. Insurance and Salvage Value	8. Deductible Loss (Enter as Item 17)
		$	$	$	$	$	$

State how property was acquired

SCHEDULE G—BAD DEBTS (See Instruction 18)

1. Year	2. Sales on Account	3. Bad Debts
1924	$	$
1925		
1926		
1927		
1928		

SCHEDULE H—DIVIDENDS DEDUCTIBLE (See Instruction 19)

1. Name of Corporation	Amount of Dividends: 2. Domestic	Amount of Dividends: 3. Foreign
	$	$

SCHEDULE I—EXPLANATION OF DEDUCTION FOR DEPRECIATION (See Instruction 20)

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquirement	5. Cost (Exclusive of Land)	6. Value as of March 1, 1913 (Exclusive of Land)	Amount of Depreciation Charged Off: 7. Previous years	Amount of Depreciation Charged Off: 8. This year
				$	$	$	$

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Attach a separate sheet if any of the above schedules do not provide sufficient space

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SCHEDULE K—BALANCE SHEETS (See Instruction 43)

Items	Beginning of Taxable Year: Amount	Beginning of Taxable Year: Total	End of Taxable Year: Amount	End of Taxable Year: Total
ASSETS				
1. Cash		$ 51 482 31		$ 43 179 57
2. Notes receivable				
3. Accounts receivable	$		$	
Less reserve for bad debts				
4. Inventories:				
Raw materials	$		$	
Work in process				
Finished goods				
Supplies				
5. Investments:				
Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	$		$	
Securities issued under the Federal Farm Loan Act, or under such Act as amended				
Obligations of the United States or its possessions				
6. Loans (describe fully):				
Installment Notes Receivable	$ 392 720 00		$ 294 540 00	
Loans to Stockholders	350 000 00		268 592 58	
		742 720 00		563 132 58
7. Deferred charges:				
Prepaid insurance	$		$	
Prepaid taxes				
8. Capital assets:				
Land				
Buildings	$		$	
Machinery and equipment				
Furniture and fixtures				
Delivery equipment				
Cost of Installment Sales	251 937 78		188 953 43	
	$		$ 188 953 43	
Less reserves for depreciation and depletion	251 937 78	251 937 78		188 953 43
9. Patents				
10. Good will				
11. Other assets (describe fully):				
Liquidating Dividends	$ 367 827 41		$ 400 179 82	
		367 827 41		400 179 82
12. Total Assets		$ 1413 967 68		$ 1185 445 40
LIABILITIES				
13. Notes payable		$		$
14. Accounts payable				
15. Accrued expenses (describe fully):				
	$		$	
16. Other liabilities (describe fully):				
Appreciation Surplus	$ 121 862 00		$ 91 396 55	
Installment Sales (Contra)	392 720 00		294 540 00	
Notes Receivable Discounted	392 720 00		294 540 00	
		907 302 00		680 476 55
17. Capital stock:				
Preferred stock (less stock in treasury)	$		$	
Common stock (less stock in treasury)	500 000 00	500 000 00	500 000 00	500 000 00
18. Surplus	$ 66 658	66 658	$ 49 685	49 685
19. Undivided profits		$ 1413 967 68		$ 1185 445 40
20. Total Liabilities				

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...CONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

1. Net income from Item 24, page 1 of the return	$ 32	488	1
2. Nontaxable income:			
(a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia			
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended			
(c) Interest on obligations of the United States or its possessions			
(d) Dividends deductible under Section 23(p) of the Revenue Act of 1924			
(e) Proceeds of life insurance policies paid upon the death of the insured			
(f) Other items of nontaxable income (to be detailed):			
(1)			
(2)			
(3)			
3. Charges against reserve for bad debts, if Item 18, page 1 of return, is not an addition to a reserve			
4. Charges against reserves for contingencies, etc. (to be detailed):			
(a)			
(b)			
(c)			
5. Total of Lines 1 to 4, inclusive	$ 32	488	14
6. Total from Line 14			
7. Net profit for year, as shown by books, before any adjustments are made therein (Line 5 minus Line 6)	$ 32	488	14
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year	6	665	58
9. Other credits to surplus (to be detailed):			
(a) 1926 Tax Refund	1	070	27
(b)			
(c)			
10. Total of Lines 7 to 9, inclusive	$ 40	223	99
11. Total from Line 17	35	255	14
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)	$ 4	968	85

13. Unallowable deductions:			
(a) Donations, gratuities, and contributions	$		
(b) Income and profits taxes paid to the United States, and so much of such taxes paid to its possessions or foreign countries as are claimed as a credit in Item 32, page 1 of the return			
(c) Federal taxes paid on tax-free covenant bonds			
(d) Special improvement taxes tending to increase the value of the property assessed			
(e) Furniture and fixtures, additions, or betterments treated as expenses on the books			
(f) Replacements and renewals			
(g) Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary			
(h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation			
(i) Additions to reserve for bad debts which are not included in Item 18, page 1 of return			
(j) Additions to reserves for contingencies, etc. (to be detailed):			
(1)			
(2)			
(3)			
(k) Other unallowable deductions (to be detailed):			
(1)			
(2)			
(3)			
14. Total of Line 13	$		
15. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property):			
(a) Date paid .... Character	$		
(b) Date paid .... Character Cash	28	589	56
(c) Date paid .... Character			
(d) Date paid .... Character			
16. Other debits to surplus (to be detailed):			
(a) 1927 Income Tax	6	665	58
(b)			
(c)			
17. Total of Lines 15 and 16	$ 35	255	14

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Alworth-Washburn Co.
vs.
David Burnet Com. & c.

QUESTIONS

KIND OF BUSINESS

1. By means of the key letters given below, identify the corporation's main income-producing activity with one of the general classes, and follow this by a special description of the business sufficient to give the information called for under each general class.

A.—Agriculture and related industries, including fishing, logging, ice harvesting, etc., and also the leasing of such property. State the product or products. B.—Mining and quarrying, including gas and oil wells, and also the leasing of such property. State the product or products. C.—Manufacturing. State the product and also the material if not implied by the name of the product. D.—Construction—excavations, buildings, bridges, railroads, ships, etc., also equipping and installing same with systems, devices, or machinery, without their manufacture. State nature of structures built, materials used, or kind of installations. E1.—Transportation—rail, water, local, etc. State the kind and special product transported, if any. E2.—Public utilities—gas (natural, coal, or water); electric light or power (hydro or steam generated); heating (steam or hot water); telephone; waterworks or power. E3.—Storage—without trading or profit from sales—(elevators, warehouses, stockyards, etc.). State product stored. E4.—Leasing transportation or utilities. State kind of property. F.—Trading in goods bought and not produced by the trading concern. State manner of trade, whether wholesale, retail, or commission, and product handled. Sales with storage with profit primarily from sales. G.—Service—domestic, including hotels, restaurants, etc.; amusements; other professional, personal, or technical service. State the service. H.—Finance, including banking, real estate, insurance. I.—Concerns not falling in above classes (a) because of combining several of them with no predominant business, or (b) for other reasons.

2. Concerns whose business involves activity falling in two or more of the above general classes, where the *same product* is concerned, should report business as identified with but one of the above general classes; for example, concerns in A or B which also transport and market their own product exclusively or mainly, should still be identified with classes A or B; concerns in C (manufacturing) which own or control their source of material supply in A or B and which also transport, sell, or install their own product exclusively or mainly, should be identified with manufacturing; concerns in D may control or own the source of supply of materials used exclusively or mainly in their constructive work; concerns in E1 or E2 may own or control the source of their material or power; concerns in F may transport or store their own merchandise, but its production would identify them with A, B, or C.

3. Answers:
(a) General class (use key letter designation) I.
(b) Main income-producing business (give specifically the information called for under each key letter, also whether acting as principal, or as agent on commission; state if inactive or in liquidation) Holding Company for Timber Investments

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTION 38

4. Does the corporation own 95 per cent or more of the outstanding capital stock of another domestic corporation or of other corporations? No

5. Is 95 per cent or more of your outstanding capital stock owned by another corporation? ....

6. Is 95 per cent or more of your outstanding capital stock as well as 95 per cent or more of the outstanding capital stock of another corporation or of other corporations owned by the same interests? No

7. If the answer to questions 4, 5, and 6, or to any of them, is "yes," answer the following:

(a) Did the corporation file Forms 851, 852, 853, and 853A for the taxable year 1924 or subsequent taxable years? No If the answer to this question is "yes," these forms will not be required, except under the circumstances described in question (b). If the answer to this question is "no," and the answer to questions 4, 5, and 6, or to any of them, is "yes," procure from the Collector of Internal Revenue for your district Forms 851, 852, 853, and 853A, Affiliations Schedules 1, 2, 3, and 4, which shall be filled in and filed as a part of this return. If the answer to this question is "no," question (b) need not be answered.

(b) Did exactly the same conditions, as are set out in the Affiliations Schedules filed for 1927 or prior years, obtain during the entire taxable year 1928? Yes If the answer to this question is "no," a statement, setting forth the particulars in which the situation has changed, should be attached to and made a part of this return. If there have been any changes in stockholdings, a complete schedule of such changes should be submitted on Form 853, Affiliations Schedule 3. If there are companies other than those covered by the Affiliations Schedules for prior years which, applying the tests contained in questions 4, 5, or 6, may have come into the affiliated group since 1927, Forms 851, 852, 853, and 853A, are required for the entire group for the taxable year.

(c) Did the corporation file a consolidated return for the preceding taxable year on a different affiliation basis from this return? No If answer is "yes," a copy of the Commissioner's letter granting permission to change the basis of filing under Section 142(a) of the Revenue Act of 1928 should be attached to the return.

PREDECESSOR BUSINESS

8. Did the corporation file a return under the same name for the preceding taxable year? Yes Was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or any prior year since December 31, 1917? — If answer is "yes," give name and address of each predecessor business, and the date of the change in entity.

Upon such change were any asset values increased or decreased? ....
If the answer is "yes," closing balance sheets of old business and opening balance sheets of new business must be furnished.

BASIS OF RETURN

9. Is this return made on the basis of actual receipts and disbursements? Yes
If not, describe fully what other basis or method was used in computing net income.

VALUATION OF INVENTORIES

10. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower. If other basis was used, describe fully, state why used and the date inventory was last reconciled with stock.

None

LIST OF ATTACHED SCHEDULES

11. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the corporation should be placed on each separate schedule accompanying the return.

The corporation's books are in care of ....
Located at ....

AFFIDAVIT

We, the undersigned, president and treasurer of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return made in good faith, for the taxable year as stated, pursuant to the Revenue Act of 1928 and the Regulations issued under authority thereof.

J. S. Washburn
President.

Phillip L. Ray
~~Treasurer.~~ Secy

Sworn to and subscribed before me this 14th day of March, 1929.

NOTARIAL SEAL

A. J. Nolan (Signature of officer administering oath), Notary Public (Title)

CORPORATE SEAL

9—1649

A. J. NOLAN
Notary Public, St. Louis Co., Minn.
My Commission Expires Jan. 30, 1935

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Alworth-Washburn Co.
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David Burnet Com. & c.

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United States of America

TREASURY DEPARTMENT
WASHINGTON

July 8 1931

PURSUANT to the provisions of Section 661, Chapter 17, Title 28 of the
d States Code (Section 882 of the Revised Statutes of the United States),
eby certify that the annexed is a true copy of the income tax return filed
rm 1120 for the year 1929 by Alworth-Washburn Company, 1600 Alworth Building,
h, Minnesota

U. S. BOARD OF TAX APPEALS
DIV. 8 DOCKET 45651
ADMITTED IN EVIDENCE
JUN 14 1931
PETITIONER'S EXHIBIT 5
RESPONDENT'S

U. S. BO... TAX APPEALS
DIV. ...KET
ADMITTED IN EVIDENCE
... 1931
PETITIONER'S EXHIBIT
RESPONDE..T

e in this Department.

IN WITNESS WHEREOF, I have hereunto set my hand, and caused the seal of the Treasury Department to be affixed, on the day and year first above written.

By direction of the Secretary of the Treasury:

F. A. Birgfeld
Chief Clerk, Treasury Department.

F.B. JaB T.B.N. JCW

Revised November, 1929—TREASURY DEPARTMENT, CHIEF CLERK AND SUPERINTENDENT.

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Alworth-Washburn Co.
vs.
David Burnet Com. & C.

TREASURY DEPARTMENT
INTERNAL REVENUE SERVICE
(Auditor's Stamp)

CORPORATION INCOME TAX RETURN
For Calendar Year 1929

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1930

Page 1 of Return

File Code 29

Serial Number 401533

(Cashier's Stamp)

NOV 17 1930

Cash Check M.O. Cert. of Ind.
First Payment
$ 996.43
Carded
As

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

Alworth-Washburn Company
(Name)
1600 Alworth Building
(Street and number)
Duluth, Minnesota
(Post office and State)

Date of Incorporation 1907

Under the Laws of what State or Country Minnesota

Kind of Business Holding Company for Real Estate and Timber Investments Is This a Consolidated Return of Two or More Corporations? No

24 1 C 9 87

Item and Instruction No.	GROSS INCOME	
1.	Gross Sales from Trading or Manufacturing, Less Returns and Allowances	$ 98,180.00
2.	Less Cost of Goods Sold:	
	(a) Inventory at beginning of year	$ —
	(b) Merchandise bought for sale	—
	(c) Cost of manufacturing or producing goods (From Schedule A)	62,984.35
	(d) Total of lines (a), (b), and (c)	$ 62,984.35
	(e) Less inventory at end of year	—
		62,984.35
3.	Gross Profit from Trading or Manufacturing (Item 1 minus Item 2)	$ 35,195.65
4.	Gross Profit from Operations Other Than Trading or Manufacturing. (State source of income):	
	(a)	—
	(b)	—
	(c)	—
5.	Interest on Bank Deposits, Notes, Mortgages, and Corporation Bonds	2,041.54
6.	Rents	—
7.	Royalties	—
8.	Profit from Sale of Real Estate, Stocks, Bonds, and other Capital Assets (From Schedule B)	—
9.	Dividends on Stock of Domestic Corporations	—
10.	Other Income (including dividends received on stock of foreign corporations). (State nature of income):	
	(a)	—
	(b)	—
	(c)	—
11.	TOTAL INCOME IN ITEMS 3 TO 10	$ 37,237.19
	DEDUCTIONS	
12.	Compensation of Officers (From Schedule C)	$ —
13.	Rent on Business Property	—
14.	Repairs (From Schedule D)	—
15.	Interest	—
16.	Taxes (From Schedule E)	352.67
17.	Losses (From Schedule F)	—
18.	Bad Debts (From Schedule G)	—
19.	Dividends (From Schedule H)	—
20.	Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule I)	—
21.	Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see Instruction 21)	—
22.	Other Deductions Not Reported Above. (Explain below, or on separate sheet):	
	(a) Salaries and wages. (Not included in Item 2, 12, or 14 above)	—
	(b) Net Loss for prior year. (Submit schedule)	—
	(c) Auditing	650.68
	(d)	—
	(e)	—
	(f)	—
23.	TOTAL DEDUCTIONS IN ITEMS 12 TO 22	$ 1,003.35
24.	NET INCOME (Item 11 minus Item 23)	$ 36,233.84

NOV 4 1930

4116

COMPUTATION OF TAX

25. Net Income (Item 24 above)	$ 36,233.84	28. Income Tax (12% of Item 27)	$ 3,985.72
26. Less Credit of $3,000 (for a domestic corporation having a net income of less than $25,360)	—	29. If net income of domestic corporation is less than $25,360, enter the amount over $25,000	—
27. Balance (Item 25 minus Item 26)	$ 36,233.84	30. Total Tax (Item 28 plus Item 29)	$ 3,985.72
31. Less: Income Tax Paid at Source. (This credit can only be allowed to a nonresident foreign corporation)	$ —		
32. Income Tax Paid to a Foreign Country or U. S. possession by a domestic corporation (see Inst. 27)	—		
33. Balance of Tax (Item 30 minus Items 31 and 32)			$ 3,985.72

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An amended return must be marked "Amended" at top of return

Checks and drafts will be accepted only if payable at par.

C

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Alworth-Washburn Co.
vs.
David Burnet Com. & C.

Items	Beginning Taxable Year — Amount	Beginning Taxable Year — Total	End Taxable Year — Amount	End Taxable Year — Total
ASSETS				
1. Cash		$ 43 177 57		$ 40 317 18
2. Notes receivable		None		None
3. Accounts receivable	$		$	
Less reserve for bad debts		None		None
4. Inventories:				
Raw materials	$		$	
Work in process				
Finished goods				
Supplies				
		None		None
5. Investments (nontaxable):				
Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	$		$	
Securities issued under the Federal Farm Loan Act, or under such Act as amended				
Obligations of the United States or its possessions		None		None
6. Other investments:				
Stocks of domestic corporations	$		$	
Bonds of domestic corporations				
Stocks and bonds of foreign corporations				
All other investments or loans		None		None
7. Deferred charges:				
Prepaid insurance	$		$	
Prepaid taxes				
All other		None		None
8. Capital assets:				
Land		None		None
Buildings	$ —		$ —	
Machinery and equipment	—		—	
Furniture and fixtures	—		—	
Delivery equipment	—		—	
	—		—	
Cost of Installment Sales	188 953 43		125 969 08	
	$ 188 953 43		$ 125 969 08	
Less reserves for depreciation	—	188 953 43	—	125 969 08
9. Patents		None		None
10. Good will		None		None
11. Other assets (describe fully):				
Installment Notes Receivable	294 540 00		$ 196 360 00	
Loans to Stockholders	258 592 58		163 526 60	
Liquidating Dividends	400 179 82	953 312 40	432 532 23	792 418 83
12. Total Assets		$ 1 185 445 40		$ 958 707 09
LIABILITIES				
13. Notes payable (less than one year)		$ None		$ None
14. Accounts payable		None		None
15. Bonds and notes (not secured by mortgage)		None		None
16. Mortgages (including bonds and notes so secured)		None		None
17. Accrued expenses:				
Interest	$		$	
Taxes				
All other		None		None
18. Other liabilities (describe fully):				
Installment Sales (Contra)	294 540 00		196 360 00	
Notes Receivable Discounted	294 540 00	589 080 00	196 360 00	392 720 00
19. Capital stock:				
Preferred stock (less stock in treasury)	$ —		$ —	
Common stock (less stock in treasury)	500 000 00	500 000 00	500 000 00	500 000 00
20. Surplus	$ 4 968 85		$ 5 055 99	
21. ~~Undivided profits~~ Appreciation Surplus	91 396 55	96 365 40	60 931 10	65 987 09
22. Total Liabilities		$ 1 185 445 40		$ 958 707 09

Remarks

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Alworth-Washburn Co.
vs.
David Burnet Com. & c.

SCHEDULE L—RECONCI TION OF NET INCOME A/ ANALYSIS OF CHANGES IN ! PLUS

1. Net income from Item 24, page 1 of the return	$ 36 233 84
2. Nontaxable income:	
(a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended	
(c) Interest on obligations of the United States or its possessions	
(d) Dividends deductible under Section 26(p) of the Revenue Act of 1928	
(e) Proceeds of life insurance policies paid upon the death of the insured	
(f) Other items of nontaxable income (to be detailed):	
(1)	
(2)	
(3)	
3. Charges against reserve for bad debts, if Item 18, page 1 of return, is not an addition to a reserve	
4. Charges against reserves for contingencies, etc. (to be detailed):	
(a)	
(b)	
(c)	
5. Total of Lines 1 to 4, inclusive	$ 36 233 84
6. Total from Line 14	
7. Net profit for year, as shown by books, before any adjustments are made therein (Line 5 minus Line 6)	$ 36 233 84
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year	4 968 85
9. Other credits to surplus (to be detailed):	
(a)	
(b)	
(c)	
10. Total of Lines 7 to 9, inclusive	$ 41 202 69
11. Total from Line 17	36 146 70
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)	$ 5 055 99

13. Unallowable deductions.	
(a) Donations, gratuities, and contributions	$
(b) Income and profits taxes paid to the United States, and so much of such taxes paid to its possessions or foreign countries as are claimed as a credit in Item 32, page 1 of the return	
(c) Federal taxes paid on tax-free covenant bonds	
(d) Special improvement taxes tending to increase the value of the property assessed	
(e) Furniture and fixtures, additions, or betterments treated as expenses on the books	
(f) Replacements and renewals	
(g) Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary	
(h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation	
(i) Additions to reserve for bad debts which are not included in Item 18, page 1 of return	
(j) Additions to reserves for contingencies, etc. (to be detailed):	
(1)	
(2)	
(3)	
(k) Other unallowable deductions (to be detailed):	
(1)	
(2)	
(3)	
14. Total of Line 13	$
15. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property):	
(a) Date paid ..... Character Cash	$ 32 248 12
(b) Date paid ..... Character	
(c) Date paid ..... Character	
(d) Date paid ..... Character	
16. Other debits to surplus (to be detailed):	
(a) Federal Income Tax, 1928	3 898 58
(b)	
(c)	
17. Total of Lines 15 and 16	$ 36 146 70

QUESTIONS

KIND OF BUSINESS

1. By means of the key letters given below, identify the corporation's main income-producing activity with one of the general classes, and follow this by a special description of the business sufficient to give the information called for under each general class.

A.—Agriculture and related industries, including fishing, logging, ice harvesting, etc., and also the leasing of such property. State the product or products. B.—Mining and quarrying, including gas and oil wells, and also the leasing of such property. State the product or products. C.—Manufacturing. State the product and also the material if not implied by the name of the product. D.—Construction—excavations, buildings, bridges, railroads, ships, etc., also equipping and installing same with systems, devices, or machinery, without their manufacture. State nature of structures built, materials used, or kind of installations. E1.—Transportation—rail, water, local, etc. State the kind and special product transported, if any. E2.—Public utilities—gas (natural, coal, or water); electric light or power (hydro or steam generated); heating (steam or hot water); telephone; waterworks or power. E3.—Storage—without trading or profit from sales—(elevators, warehouses, stockyards, etc.). State product stored. E4.—Leasing transportation or utilities. State kind of property. F.—Trading in goods bought and not produced by the trading concern. State manner of trade, whether wholesale, retail, or commission, and product handled. Sales with storage with profit primarily from sales. G.—Service—domestic, including hotels, restaurants, etc.; amusements; other professional, personal, or technical service. State the service. H.—Finance, including banking, real estate, insurance. I.—Concerns not falling in above classes (a) because of combining several of them with no predominant business, or (b) for other reasons.

2. Concerns whose business involves activity falling in two or more of the above general classes, where the *same product* is concerned, should report business as identified with but one of the above general classes; for example, concerns in A or B which also transport and market their own product exclusively or mainly, should still be identified with classes A or B; concerns in C (manufacturing) which own or control their source of material supply in A or B and which also transport, sell, or install their own product exclusively or mainly, should be identified with manufacturing; concerns in D may control or own the source of supply of materials used exclusively or mainly in their constructive work; concerns in E1 or E2 may own or control the source of their material or power; concerns in F may transport or store their own merchandise, but its production would identify them with A, B, or C.

3. Answers:

(a) General class (use key letter designation) I

(b) Main income-producing business (give specifically the information called for under each key letter, also whether acting as principal, or as agent on commission; state if inactive or in liquidation)

Holding Company for Real Estate and Timber Investments

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTION 38

4. Is this a consolidated return of two or more corporations? No

If so, procure from the Collector of Internal Revenue for your district Form 851, Affiliations Schedule, which shall be filled in, sworn to, and filed as a part of this return. See Article 12 (c) and (d), Regulations 75.

5. Did the corporation file a consolidated return for the preceding taxable year? No

PREDECESSOR BUSINESS

6. Did the corporation file a return under the same name for the preceding taxable year? Yes Was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or any prior year since December 31, 1917? No If answer is "yes," give name and address of each predecessor business, and the date of the change in entity. ✓

Upon such change were any asset values increased or decreased? ✓

If the answer is "yes," closing balance sheets of old business and opening balance sheets of new business must be furnished.

BASIS OF RETURN

7. Is this return made on the basis of actual receipts and disbursements? Yes

If not, describe fully what other basis or method was used in computing net income. ✓

VALUATION OF INVENTORIES

8. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower. If other basis was used, describe fully, state why used and the date inventory was last reconciled with stock.

None

LIST OF ATTACHED SCHEDULES

9. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the corporation should be placed on each separate schedule accompanying the return.

None

The corporation's books are in care of Frank H. Wilson

Located at 516 Providence Bldg., Duluth, Minn.

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Alworth-Washburn Co.
vs.
David Burnet Com. & C.

Items	Amount	Items	Amount (Enter as Item 20)
Salaries and wages	$	Total Sale Price $584,38.02	$
Material and supplies		$98,180.00 collected in 1929 in 16.6735%	
		16.6735% of Total Cost $377,751.23 is	62,984.35

SCHEDULE B—PROFIT FROM SALE OF REAL ESTATE, STOCKS, BONDS, ETC. (See Instruction 8)

1. Kind of Property	2. Date Acquired	3. Amount Received	4. Depreciation Allowable Since Acquisition	5. Cost or Value as of March 1, 1913, Whichever Greater	6. Subsequent Improvements	7. Net Profit (Enter as Item 8)
		$	$	$	$	$
					None	

State how property was acquired

SCHEDULE C—COMPENSATION OF OFFICERS (See Instruction 12)

1. Name of Officer	2. Official Title	3. Time Devoted to Business	Shares of Stock Owned 4. Common	5. Preferred	6. Amount of Compensation (Enter as Item 12)
					$
				None	

SCHEDULE D—COST OF REPAIRS (See Instruction 14)

1. Items	2. Amount (Enter as Item 14)
Salaries and wages	$
None	

SCHEDULE E—TAXES PAID (See Instruction 16)

1. Items	2. Amount (Enter as Item 16)
Annual License Fee	$ 200.00
Personal Property + Money + Credits	142.67
U.S. Board of Tax Appeals	10.00
	352.67

SCHEDULE F—EXPLANATION OF LOSSES BY FIRE, STORM, ETC. (See Instruction 17)

1. Kind of Property	2. Date Acquired	3. Cost or Value as of March 1, 1913, Whichever Greater	4. Subsequent Improvements	5. Depreciation Allowable Since Acquisition	6. Insurance and Salvage Value	7. Deductible Loss (Enter as Item 17)
		$	$	$	$	$
					None	

State how property was acquired

SCHEDULE G—BAD DEBTS (See Instruction 18)

1. Year	2. Sales on Account	3. Bad Debts
1925	$	$
1926		
1927	None	
1928		
1929		

SCHEDULE H—DIVIDENDS DEDUCTIBLE (See Instruction 19)

1. Name of Corporation	Amount of Dividends 2. Domestic	3. Foreign
	$	$
	None	

SCHEDULE I—EXPLANATION OF DEDUCTION FOR DEPRECIATION (See Instruction 20)

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquirement	5. Cost or Value as of March 1, 1913, Whichever Greater (Exclusive of Land)	Amount of Depreciation Charged Off 6. Previous years	7. This year
				$	$	$
5858. Alworth-Washburn Co. vs. David Burnet, Com. & C.					None	

AFFIDAVIT

We, the undersigned, president and treasurer of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return made in good faith, for the taxable year stated, pursuant to the Revenue Act of 1928 and the Regulations issued thereunder.

Sworn to and subscribed before me this 13th day of March, 1930.

NOTARIAL SEAL

A. J. Nolan, (Signature of officer administering oath) (Title)

CORPORATE SEAL

J. Washburn, President

Attach a separate sheet if any of the above schedules do not provide sufficient space

2—15166

A. J. NOLAN
Notary Public St. Louis Co., Minn.
My Commission Expires Jan. 30, 1936

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5858
Alworth-Washburn Co.
vs.
David Burnet Com. & C.

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Form 1120
TREASURY DEPARTMENT
INTERNAL REVENUE SERVICE
(Auditor's Stamp)

CORPORATION INCOME TAX RETURN
For Calendar Year 1930

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1931

Page 1 of Return

File Code .....

Serial Number .....

District .....
(Cashier's Stamp)

Cash Check M.O. Cert. of Ind.
First Payment
$ .....

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

ALWORTH-WASHBURN COMPANY.
(Name)

1600 Alworth Building
(Street and number)

Duluth, Minnesota.
(Post office and State)

Date of Incorporation 1907

Under the Laws of what State or Country Minnesota

Kind of Business Holding Company for Timber Investments Is This a Consolidated Return of Two or More Corporations? No If so, How Many? -

Item and Instruction No.										
	GROSS INCOME									
1.	Gross Sales from Trading or Manufacturing, $ 98,180.00; Less Returns and Allowances, $ -; Net Sales				$	98	180	00		
2.	Less Cost of Goods Sold:									
	(a) Inventory at beginning of year	$		-						
	(b) Merchandise bought for sale			-						
	(c) Cost of manufacturing or producing goods (From Schedule A): Salaries and Wages, $; Other costs, $ 62,984.35; Total		62	984	35					
	(d) Total of lines (a), (b), and (c)	$	62	984	35					
	(e) Less inventory at end of year			-		62	984	35		
3.	Gross Profit from Trading or Manufacturing (Item 1 minus Item 2)				$	35	195	65		
4.	Gross Profit from Operations Other Than Trading or Manufacturing. (State source of income)									
	(a)						-			
	(b)						-			
	(c)						-			
5.	Interest on Bank Deposits, Notes, Mortgages, and Corporation Bonds					1	172	26		
6.	Rents						-			
7.	Royalties						-			
8.	Profit from Sale of Real Estate, Stocks, Bonds, and other Capital Assets (From Schedule B)						-			
9.	Dividends on Stock of Domestic Corporations						-			
10.	Other Income (including dividends received on Stock of foreign corporations). (State nature of income):						-			
	(a)						-			
	(b)						-			
	(c)						-			
11.	TOTAL INCOME IN ITEMS 3 TO 10								$	36 367 91
	DEDUCTIONS									
12.	Compensation of Officers (From Schedule C)						-			
13.	Rent on Business Property						-			
14.	Repairs (From Schudle D); Salaries and Wages, $; Other Costs, $; Total						-			
15.	Interest						-			
16.	Taxes (From Schedule E)						329	41		
17.	Losses (From Schedule F)						-			
18.	Bad Debts (From Schedule G)						-			
19.	Dividends (From Schedule H)						-			
20.	Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule I)						-			
21.	Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see Instruction 21)						-			
22.	Other Deductions Not Reported Above. (Explain below, or on separate sheet):									
	(a) Salaries and wages. (Not included in Item 2, 12, or 14 above)						-			
	(b) Net Loss for 1928-1929 (Submit schedule)						-			
	(c) Auditing					1	002	87		
	(d) Miscellaneous						3	26		
	(e)						-			
23.	TOTAL DEDUCTIONS IN ITEMS 12 TO 22								$	1 335 54
24.	NET INCOME (Item 11 minus Item 23)								$	35 032 37

U.S. BOARD OF TAX APPEALS
DIV. 8 DOCKET 45651
ADMITTED IN EVIDENCE
JUN 1 1 1931
PETITIONER'S EXHIBIT 6
RESPONDENT'S

COMPUTATION OF TAX

25. Net Income (Item 24 above)	$	35	032	37	28. Income Tax (12% of Item 27)	$	4	203	88
26. Less Credit of $3,000 (for a domestic corporation having a net income of less than $25,360)			-		29. If net income of domestic corporation is less than $25,360, enter the amount over $25,000			-	
27. Balance (Item 25 minus Item 26)	$	35	032	37	30. Total Tax (Item 28 plus Item 29)	$	4	203	88
31. Less: Income Tax Paid at Source. (This credit can only be allowed to a nonresident foreign corporation)					$ -				
32. Income Tax Paid to a Foreign Country or U. S. possession by a domestic corporation (see Inst. 27)					-		4	203	88
33. Balance of Tax (Item 30 minus Items 31 and 32)						$			

An amended return must be marked "Amended" at top of return **Checks and drafts will be accepted only if payable at par**

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Page 2 of Return

SCHEDULE K—BALANCE SHEETS (See Instruction 43)

Items	Beginning of Taxable Year: Amount	Beginning of Taxable Year: Total	End of Taxable Year: Amount	End of Taxable Year: Total
ASSETS				
1. Cash		$ 40 319 18		$ 36 170 18
2. Notes receivable				
3. Accounts receivable	$		$	
Less reserve for bad debts				
4. Inventories:				
Raw materials	$		$	
Work in process				
Finished goods				
Supplies				
5. Investments (nontaxable): Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	$		$	
Securities issued under the Federal Farm Loan Act, or under such Act as amended				
Obligations of the United States or its possessions				
6. Other investments:				
Stocks of domestic corporations	$		$	
Bonds of domestic corporations				
Stocks and bonds of foreign corporations				
All other investments or loans				
7. Deferred charges:				
Prepaid insurance	$		$	
Prepaid taxes				
All other				
8. Capital assets:				
Land				
Buildings	$		$	
Machinery and equipment				
Furniture and fixtures				
Delivery equipment				
	$		$	
Less reserves for depreciation				
9. Patents				
10. Good will ~~Cost of Installment Sales~~	125 969 08		62 984 73	
11. Other assets (describe fully):				
~~Installment Notes Receivable~~	196 360 00		$ 98 180 00	
~~Loans to Stockholders~~	163 526 60		69 380 78	
~~Liquidating Dividends~~	432 532 23	918 387 91	465 384 11	695 929 62
12. Total Assets		$ 958 707 09		$ 732 099 80
LIABILITIES				
13. Notes payable (less than one year)		$		$
14. Accounts payable				
15. Bonds and notes (not secured by mortgage)				
16. Mortgages (including bonds and notes so secured)				
17. Accrued expenses:				
Interest	$		$	
Taxes				
All other				
18. Other liabilities (describe fully):				
~~Installment Sales~~	196 360 00		98 180 00	
~~Notes Receivable Discounted~~ (Contra)	196 360 00	392 720 00	98 180 00	196 360 00
19. Capital stock:				
Preferred stock (less stock in treasury)	$		$	
Common stock (less stock in treasury)	500 000 00	500 000 00	500 000 00	500 000 00
20. Surplus	$ 5 055 99		$ 5 274 15	
21. Undivided ~~Profits~~ Appreciation Surplus	60 931 10	65 987 09	30 465 65	35 739 80
22. Total Liabilities		$ 958 707 09		$ 732 099 80

Remarks

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SCHEDULE L—RECONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

1. Net income from Item 24, page 1 of the return	$ 35 032 37	
2. Nontaxable income:		
(a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia		—
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended		—
(c) Interest on obligations of the United States or its possessions		—
(d) Dividends deductible under Section 23(p) of the Revenue Act of 1928		—
(e) Proceeds of life insurance policies paid upon the death of the insured		—
(f) Other items of nontaxable income (to be detailed):		
(1)		—
(2)		—
(3)		—
3. Charges against reserve for bad debts, if Item 18, page 1 of return, is not an addition to a reserve		—
4. Charges against reserves for contingencies, etc. (to be detailed):		
(a)		—
(b)		—
(c)		—
5. Total of Lines 1 to 4, inclusive	$ 35 032 37	
6. Total from Line 14		—
7. Net profit for year, as shown by books, before any adjustments are made therein (Line 5 minus Line 6)	$ 35 032 37	
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year	5 055 99	
9. Other credits to surplus (to be detailed):		
(a)		—
(b)		—
(c)		—
10. Total of Lines 7 to 9, inclusive	$ 40 088 36	
11. Total from Line 17	34 814 21	
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)	$ 5 274 15	

13. Unallowable deductions:		
(a) Donations, gratuities, and contributions	$	—
(b) Income and profits taxes paid to the United States, and so much of such taxes paid to its possessions or foreign countries as are claimed as a credit in Item 32, page 1 of the return		—
(c) Federal taxes paid on tax-free covenant bonds		—
(d) Special improvement taxes tending to increase the value of the property assessed		—
(e) Furniture and fixtures, additions, or betterments treated as expenses on the books		—
(f) Replacements and renewals		—
(g) Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary		—
(h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation		—
(i) Additions to reserve for bad debts which are not included in Item 18, page 1 of return		—
(j) Additions to reserves for contingencies, etc. (to be detailed):		
(1)		—
(2)		—
(3)		—
(k) Other unallowable deductions (to be detailed):		
(1)		—
(2)		—
(3)		—
14. Total of Line 13	$	—
15. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property):		
(a) Date paid ..... Character Cash	$ 30 828 49	
(b) Date paid ..... Character		—
(c) Date paid ..... Character		—
(d) Date paid ..... Character		—
16. Other debits to surplus (to be detailed):		
(a) Federal Income Tax 1929	3 985 72	
(b)		—
(c)		—
17. Total of Lines 15 and 16	$ 34 814 21	

QUESTIONS

KIND OF BUSINESS

1. By means of the key letters given below, identify the corporation's main income-producing activity with one of the general classes, and follow this by a special description of the business sufficient to give the information called for under each general class.

A.—Agriculture and related industries, including fishing, logging, ice harvesting, etc., and also the leasing of such property. State the product or products. B.—Mining and quarrying, including gas and oil wells, and also the leasing of such property. State the product or products. C.—Manufacturing. State the product and also the material if not implied by the name of the product. D.—Construction—excavations, buildings, bridges, railroads, ships, etc., also equipping and installing same with systems, devices, or machinery, without their manufacture. State nature of structures built, materials used, or kind of installations. E1.—Transportation—rail, water, local, etc. State the kind and special product transported, if any. E2.—Public utilities—gas (natural, coal, or water); electric light or power (hydro or steam generated); heating (steam or hot water); telephone; waterworks or power. E3.—Storage—without trading or profit from sales—(elevators, warehouses, stockyards, etc.). State product stored. E4.—Leasing transportation or utilities. State kind of property. F.—Trading in goods bought and not produced by the trading concern. State manner of trade, whether wholesale, retail, or commission, and product handled. Sales with storage with profit primarily from sales. G.—Service—domestic, including hotels, restaurants, etc.; amusements; other professional, personal, or technical service. State the service. H.—Finance, including banking, real estate, insurance. I.—Concerns not falling in above classes (a) because of combining several of them with no predominant business, or (b) for other reasons.

2. Concerns whose business involves activity falling in two or more of the above general classes, where the *same product* is concerned, should report business as identified with but one of the above general classes; for example, concerns in A or B which also transport and market their own product exclusively or mainly, should still be identified with classes A or B; concerns in C (manufacturing) which own or control their source of material supply in A or B and which also transport, sell, or install their own product exclusively or mainly, should be identified with manufacturing; concerns in D may control or own the source of supply of materials used exclusively or mainly in their constructive work; concerns in E1 or E2 may own or control the source of their material or power; concerns in F may transport or store their own merchandise, but its production would identify them with A, B, or C.

3. Answers:

(a) General class (use key letter designation) I

(b) Main income-producing business (give specifically the information called for under each key letter, also whether acting as principal, or as agent on commission; state if inactive or in liquidation)

Holding Company for Timber Investments
Inactive - Principal

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTION 36

4. Is this a consolidated return of two or more corporations? No

If so, procure from the Collector of Internal Revenue for your district Form 851, Affiliations Schedule, which shall be filled in, sworn to, and filed as a part of this return. See Article 12 (c) and (d), Regulations 75.

5. Did the corporation file a consolidated return for the preceding taxable year? No

PREDECESSOR BUSINESS

6. Did the corporation file a return under the same name for the preceding taxable year? Yes Was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or any prior year since December 31, 1917? No If answer is "yes," give name and address of each predecessor business, and the date of the change in entity. —

Upon such change were any asset values increased or decreased? —

If the answer is "yes," closing balance sheets of old business and opening balance sheets of new business must be furnished.

BASIS OF RETURN

7. Is this return made on the basis of actual receipts and disbursements? Yes

If not, describe fully what other basis or method was used in computing net income. —

VALUATION OF INVENTORIES

8. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower. If other basis was used, describe fully, state why used and the date inventory was last reconciled with stock. —

LIST OF ATTACHED SCHEDULES

9. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the corporation should be placed on each separate schedule accompanying the return.

None

The corporation's books are in care of

Located at

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Page 4 of Return

SCHEDULE A—COST OF MANUFACTURING OR PRODUCING GOODS (See Instruction 2)

Items	Amount	Items	Amount (Enter as Item 2c)
Salaries and wages	$ /		$
Material and supplies			
Total Sale Price $588,838.02			
$98,180.00 collected in 1930 is			
16.6735%			
16.6735% of total cost $377,751.23			
	62,984 35		

SCHEDULE B—PROFIT FROM SALE OF REAL ESTATE, STOCKS, BONDS, ETC. (See Instruction 8)

1. Kind of Property	2. Date Acquired	3. Amount Realized	4. Depreciation Allowable Since Acquisition	5. Cost or Value as of March 1, 1913, Whichever Greater	6. Subsequent Improvements	7. Net Profit (Enter as Item 8)
		$	$	$	$	$
						None

State how property was acquired

SCHEDULE C—COMPENSATION OF OFFICERS (See Instruction 12)

1. Name of Officer	2. Official Title	3. Time Devoted to Business	Shares of Stock Owned 4. Common	Shares of Stock Owned 5. Preferred	6. Amount of Compensation (Enter as Item 12)
					$
					None

SCHEDULE D—COST OF REPAIRS (See Instruction 14)

1. Items	2. Amount (Enter as Item 14)
Salaries and wages	$
	None

SCHEDULE E—TAXES PAID (See Instruction 16)

1. Items	2. Amount (Enter as Item 16)
Money & Credits Tax	$ 129 41
Oregon Annual License	200 00
	329 41

SCHEDULE F—EXPLANATION OF LOSSES BY FIRE, STORM, ETC. (See Instruction 17)

1. Kind of Property	2. Date Acquired	3. Cost or Value as of March 1, 1913, Whichever Greater	4. Subsequent Improvements	5. Depreciation Allowable Since Acquisition	6. Insurance and Salvage Value	7. Deductible Loss (Enter as Item 17)
		$	$	$	$	$
						None

State how property was acquired

SCHEDULE G—BAD DEBTS (See Instruction 18)

1. Year	2. Sales on Account	3. Bad Debts
1926	$	$
1927		
1928		
1929		
1930		None

SCHEDULE H—DIVIDENDS DEDUCTIBLE (See Instruction 19)

1. Name of Corporation	Amount of Dividends 2. Domestic	Amount of Dividends 3. Foreign
	$	$
		None

SCHEDULE I—EXPLANATION OF DEDUCTION FOR DEPRECIATION (See Instruction 20)

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquirement	5. Cost or Value as of March 1, 1913, Whichever Greater (Exclusive of Land)	Amount of Depreciation Charged Off 6. Previous years	7. This year
				$	$	$
						None

AFFIDAVIT

We, the undersigned, president and treasurer of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return made in good faith, for the taxable year stated, pursuant to the Revenue Act of 1928 and the Regulations issued thereunder.

Sworn to and subscribed before me this ..... day of ....., 1931.

NOTARIAL SEAL

..... (Signature of officer administering oath), ... (Title)

CORPORATE SEAL

J. Washburn
President.
Asa Bilda
Asst. Treasurer.

Attach a separate sheet if any of the above schedules do not provide sufficient space

9—15468

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Alworth-Washburn Co.
vs.
David Burnet Com. & C.

OK Computation proved 105589 **FIELD AUDIT** C. R. 29 Nicholson

Form 1120
U. S. Internal Revenue
(Audit [illegible], Title
ASSESSMENT

Tax 19,005.60
Penalty
Interest
Total
Basic [illegible] 9/11/29
Added by Owen 6/27 1929
Unit No. AR 07
List
Page Line

CORPORATION INCOME TAX RETURN
For Calendar Year 1927

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1928

Page 1 of Return
File Code 19
Serial Number 401803
(Cashier's Stamp)

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

ALWORTH-WASHBURN COMPANY
(Name)
1600 ALWORTH BUILDING
(Street and Number)
DULUTH MINNESOTA
(Post office and State)

Date of Incorporation 1907
Under the Laws of what State or Country Minnesota

Cash Check M. O. Cert. of Ind.
First Payment 1666.39
Carded
As

KIND OF BUSINESS Holding Company for Real Estate and Timber Investments IS THIS A CONSOLIDATED RETURN? No

8

RECEIVED JUL 30 Internal Revenue Agent in Charge St. Paul Division

RECEIVED APR 3 1929 Office of Head AUDIT REVIEW DIVISION

U. S. BOARD OF TAX APPEALS DIV. 8 DOCKET 45651 ADMITTED IN EVIDENCE JUN 14 1931 PETITIONER'S Joint EXHIBIT A-7 RESPONDENT'S

RECEIVED WITH REMITTANCE Collector of Internal Revenue District of Minnesota MAR 15 1928 St. Paul Main Office

GROSS INCOME

Items and Instructions No.		
1. Gross Sales from Trading or Manufacturing, Less Returns and Allowances		$ 75,000.00
2. Less Cost of Goods Sold:		
(a) Inventory at close of preceding year		
(b) Merchandise bought for sale		
(c) Cost of manufacturing or otherwise producing goods (From Schedule A)	48,113.80	
(d) Total of lines (a), (b), and (c)	48,113.80	
(e) Less inventory at end of year		48,113.80
3. Gross Profit from Trading or Manufacturing (Item 1 minus Item 2)		$ 26,886.20
4. Gross Profit from Operations Other Than Trading or Manufacturing. (State source of income):		
(a)		
(b)		
(c)		
5. Interest on Bank Deposits, Notes, Mortgages, and Corporation Bonds		54,847.00
6. Rents		
7. Royalties		
8. Profit from Sale of Real Estate, Stocks, Bonds, and other Capital Assets (From Schedule B)		
9. Dividends on Stock of Domestic Corporations		
10. Other Income (including dividends received on stock of foreign corporations). (State nature of income):		
(a)		
(b)		
(c)		
11. Total Income in Items 3 to 10		$ 81,733.20

DEDUCTIONS

12. Compensation of Officers (From Schedule C)	300.00	
13. Rent on Business Property		
14. Repairs (From Schedule D)		
15. Interest	20,654.08	
16. Taxes (From Schedule E)	231	
17. Losses by Fire, Storm, etc. (From Schedule F)		
18. Bad Debts (From Schedule G)		
19. Dividends (From Schedule H)		
20. Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule I)		
21. Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see Instruction 21)		
22. Other Deductions Not Reported Above. (Explain below, or on separate sheet):		
(a) Salaries and wages. (Not included in Item 2, 12, or 14 above)		
(b) Net Loss for prior year. (Submit schedule)		
(c) Auditing	585.00	
(d) Commissions	10,617.14	
(e) License, State of Oregon	200.00	
(f)		
23. Total Deductions in Items 12 to 22		$ 32,358.53
24. Net Income (Item 11 minus Item 23)		$ 49,374.67

COMPUTATION OF TAX

25. Net Income (Item 24 above)	$ 49,374.67	28. Income Tax (13½% of Item 27)	$ 6,665.58
26. Less Credit of $2,000 (for a domestic corporation having a net income of less than $25,270)		29. If the Net Income of a Domestic Corporation is Less Than $25,270, Enter the Amount in Excess of $25,000	
27. Balance (Item 25 minus Item 26)	$ 49,374.67	30. Total Tax (Item 28 plus Item 29)	$ 6,665.58
31. Less: Income Tax Paid at Source. (This credit can only be allowed to a nonresident foreign corporation)		$	
32. Income and Profits Taxes Paid to a Foreign Country or to a Possession of the United States by a domestic corporation			
33. Balance of Tax (Item 30 minus Items 31 and 32)			$ 6,665.58

An amended return must be marked "Amended" at top of return

Checks and drafts will be accepted only if payable domestic

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Alworth-Washburn Co.
vs.
David Burnet Com. & C.

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Page 3 of Return

SCHEDULE K—BALANCE SHEETS (See Instruction 43)

Items	Beginning of Taxable Year: Amount	Beginning of Taxable Year: Total	End of Taxable Year: Amount	End of Taxable Year: Total
ASSETS				
1. Cash		$ 6891.30		$ 51482.39
2. Notes receivable				
3. Accounts receivable	$		$	
Less reserve for bad debts				
4. Inventories:				
Raw materials	$		$	
Work in process				
Finished goods				
Supplies				
5. Investments:				
Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	$		$	
Securities issued under the Federal Farm Loan Act, or under such Act as amended				
Obligations of the United States or its possessions				
6. Loans (describe fully):				
Installment Notes Receivable	$ 467720.00		$ 392720.00	
Loans to Stockholders			350000.00	
		467720.00		742720.00
7. Deferred charges:				
Prepaid insurance	$		$	
Prepaid taxes				
8. Capital assets:				
Land				
Buildings	$		$	
Machinery and equipment				
Furniture and fixtures				
Delivery equipment				
Cost of Installment Sales	300051.58		251937.78	
	$ 300051.58		$ 251937.78	
Less reserves for depreciation and depletion		300051.58		251937.78
9. Patents				
10. Good will				
11. Other assets (describe fully):				
Liquidating Dividends	$ 365598.12		$ 367827.41	
		365598.12		367827.41
12. Total Assets		$ 1140261.00		$ 1413967.58
LIABILITIES				
13. Notes payable		$		$
14. Accounts payable				
15. Accrued expenses (describe fully):				
	$		$	
16. Other liabilities (describe fully):				
Appreciation Surplus	$ 145134.58		$ 121862.00	
Installment Sales (contra)	467720.00		392720.00	
Notes Receivable Discounted			392720.00	
		612854.58		907302.00
17. Capital stock:				
Preferred stock (less stock in treasury)	$		$	
Common stock (less stock in treasury)	500000.00	500000.00	500000.00	500000.00
18. Surplus	$ 27406.42		$ 6665.58	
19. Undivided profits		27406.42		6665.58
20. Total Liabilities		$ 1140261.00		$ 1413967.58

Remarks

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Alworth-Washburn Co.
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TREASURY DEPARTMENT
INTERNAL REVENUE BUREAU
Form 7872—Jan., 1926

31

INTEREST PAID ON REFUND OR CREDIT OF INCOME TAX

RECEIVED
Internal Revenue
St. Paul Division

Auditor will definitely ascertain that the amount of interest shown hereon has been included in taxable income for the year in which received

Schedule No. IT- 23653

Date check mailed

CHARGE RECORD

Return charged to

Date , 192

Form

Name Alworth-Washburn Co.

Street c/o Frank G. Wilson

City Duluth State Minnesota Dist. Minnesota

AMOUNT REFUNDED	AMOUNT CREDITED	INTEREST PAID
$ 3195.98	$	$ 423.58

Credited to Acct. L pp 112

NOTE.—This certificate must be stapled or securely pinned to the return and not removed therefrom.

GOVERNMENT PRINTING OFFICE 2-18341

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Alworth-Washburn Co.
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Page 2 of Return — **SCHEDULE A—COST OF MANUFACTURING OR PRODUCING GOODS** (See Instruction 2)

Items	Amount	Items	Amount (Enter as Item 2c)
Salaries and wages	$	Fair Value Nonkiser Droop I.T.C.A. 2554-17	$339,209.51
Material and supplies		Carrying charges 3-1-13 to 12-31-22 (prorated)	38541.72
		Total	$377,751.23
		Total Sales from $588,838.02	
		$75,000.00 collected in 1927 is 12.73699%	
		12.73699% of book $377,751.23	48,113.80

SCHEDULE B—PROFIT FROM SALE OF REAL ESTATE, STOCKS, BONDS, ETC. (See Instruction 8)

1. Kind of Property	2. Date Acquired	3. Amount Received	4. Depreciation Allowable Since Acquisition	5. Cost	6. Value as of March 1, 1913	7. Subsequent Improvements	8. Net Profit (Enter as Item 8)
		$	$	$	$	$	$
							None

State how property was acquired

SCHEDULE C—COMPENSATION OF OFFICERS (See Instruction 12)

1. Name of Officer	2. Official Title	3. Time Devoted to Business	Shares of Stock Owned: 4. Common	Shares of Stock Owned: 5. Preferred	6. Amount of Compensation (Enter as Item 12)
Philip K. Ray	Secy-Treas.	Part	11		$ 300.00

SCHEDULE D—COST OF REPAIRS (See Instruction 14)

1. Items	2. Amount (Enter as Item 14)
Salaries and wages	$

SCHEDULE E—TAXES PAID (See Instruction 16)

1. Items	2. Amount (Enter as Item 16)
Personal Property	$ 2.31

SCHEDULE F—EXPLANATION OF LOSSES BY FIRE, STORM, ETC. (See Instruction 17)

1. Kind of Property	2. Date Acquired	3. Cost	4. Value as of March 1, 1913	5. Subsequent Improvements	6. Depreciation Allowable Since Acquisition	7. Insurance and Salvage Value	8. Net Loss (Enter as Item 17)
		$	$	$	$	$	$
							None

State how property was acquired

SCHEDULE G—BAD DEBTS (See Instruction 18)

1. Year	2. Sales on Account	3. Bad Debts
1922	$	$
1923		
1924		
1925		None
1926		

SCHEDULE H—DIVIDENDS DEDUCTIBLE (See Instruction 19)

1. Name of Corporation	Amount of Dividends: 2. Domestic	Amount of Dividends: 3. Foreign
	$	$
		None

SCHEDULE I—EXPLANATION OF DEDUCTION FOR DEPRECIATION (See Instruction 20)

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquirement	5. Cost (Exclusive of Land)	6. Value as of March 1, 1913 (Exclusive of Land)	Amount of Depreciation Charged Off: 7. Previous years	Amount of Depreciation Charged Off: 8. This year
				$	$	$	$
							None

Attach a separate sheet if any of the above schedules do not provide sufficient space

2—14448

79

33

5858
Alworth-Washburn Co.
vs.
David Burnet Com. & Co.

SCHEDULE L—RECONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

1. Net income from Item 21, page 1 of the return	$	49,374 67
2. Nontaxable income:		
(a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia		
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended		
(c) Interest on obligations of the United States or its possessions		
(d) Dividends deductible under Section 234(a) 6 of the Revenue Act of 1926		
(e) Proceeds of life insurance policies paid upon the death of the insured		
(f) Other items of nontaxable income (to be detailed):		
(1)		
(2)		
(3)		
3. Charges against reserve for bad debts, if Item 18, page 1 of return, is not an addition to a reserve		
4. Charges against reserves for contingencies, etc. (to be detailed):		
(a)		
(b)		
(c)		
5. Total of Lines 1 to 4, inclusive	$	49,374 67
6. Total from Line 14		
7. Net profit for year as shown by books, before any adjustments are made therein (Line 5 minus Line 6)	$	49,374 67
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year		27,406 42
9. Other credits to surplus (to be detailed):		
(a) 1923 Income tax refund	Cr.	3,195 98
(b)		
(c)		
10. Total of Lines 7 to 9, inclusive	$	79,977 07
11. Total from Line 17		73,311 49
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)	$	6,665 58

13. Unallowable deductions:		
(a) Donations, gratuities, and contributions	$	
(b) Income and profits taxes paid to the United States, and so much of such taxes paid to its possessions or foreign countries as are claimed as a credit in Item 32, page 1 of the return		
(c) Federal taxes paid on tax-free covenant bonds		
(d) Special improvement taxes tending to increase the value of the property assessed		
(e) Furniture and fixtures, additions, or betterments treated as expenses on the books		
(f) Replacements and renewals		
(g) Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary		
(h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation		
(i) Additions to reserve for bad debts which are not included in Item 18, page 1 of return		
(j) Additions to reserves for contingencies, etc. (to be detailed):		
(1)		
(2)		
(3)		
(k) Other unallowable deductions (to be detailed):		
(1)		
(2)		
(3)		
14. Total of Line 13	$	
15. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property):		
(a) Date paid .... Character cash		44,498 13
(b) Date paid .... Character		
(c) Date paid .... Character		
(d) Date paid .... Character		
16. Other debits to surplus (to be detailed):		
(a) Income tax 1926		27,406 42
(b) Add'l 1924 Income tax		1,406 94
(c)		
17. Total of Lines 15 and 16	$	73,311 49

QUESTIONS

KIND OF BUSINESS

1. By means of the key letters given below, identify the corporation's main income-producing activity with one of the general classes, and follow this by a special description of the business sufficient to give the information called for under each general class.

A.—Agriculture and related industries, including fishing, logging, ice harvesting, etc., and also the leasing of such property. State the product or products. B.—Mining and quarrying, including gas and oil wells, and also the leasing of such property. State the product or products. C.—Manufacturing. State the product and also the material if not implied by the name of the product. D.—Construction—excavations, buildings, bridges, railroads, ships, etc., also equipping and installing same with systems, devices, or machinery, without their manufacture. State nature of structures built, materials used, or kind of installations. E1.—Transportation—rail, water, local, etc. State the kind and special product transported, if any. E2.—Public utilities—gas (natural, coal, or water); electric light or power (hydro or steam generated); heating (steam or hot water); telephone; waterworks or power. E3.—Storage—without trading or profit from sales—(elevators, warehouses, stockyards, etc.). State product stored. E4.—Leasing transportation or utilities. State kind of property. F.—Trading in goods bought and not produced by the trading concern. State manner of trade, whether wholesale, retail, or commission, and product handled. Sales with storage with profit primarily from sales. G.—Service—domestic, including hotels, restaurants, etc.; amusements; other professional, personal, or technical service. State the service. H.—Finance, including banking, real estate, insurance. I.—Concerns not falling in above classes (a) because of combining several of them with no predominant business, or (b) for other reasons.

2. Concerns whose business involves activity falling in two or more of the above general classes, where the *same product* is concerned, should report business as identified with but one of the above general classes; for example, concerns in A or B which also transport and market their own product exclusively or mainly, should still be identified with classes A or B; concerns in C (manufacturing) which own or control their source of material supply in A or B and which also transport, sell, or install their own product exclusively or mainly, should be identified with manufacturing; concerns in D may control or own the source of supply of materials used exclusively or mainly in their constructive work; concerns in E1 or E2 may own or control the source of their material or power; concerns in F may transport or store their own merchandise, but its production would identify them with A, B, or C.

3. Answers:
(a) General class (use key letter designation) I
(b) Main income-producing business (give specifically the information called for under each key letter, also whether acting as principal, or as agent on commission; state if inactive or in liquidation)
Holding Company for Timber Investments

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTION 38

4. Does the corporation own 95 per cent or more of the outstanding capital stock of another domestic corporation or of other corporations? No

5. Is over 95 per cent or more of your outstanding capital stock owned by another corporation? No

6. Is 95 per cent or more of your outstanding capital stock as well as 95 per cent or more of the outstanding capital stock of another corporation or of other corporations owned or controlled by the same individual or partnership or by the same individuals, partnerships, or corporations in substantially the same proportion? No

7. If the answer to questions 4, 5, and 6, or to any of them, is "yes," answer the following:
(a) Did the corporation file Forms 851, 852, 853, and 853A for the taxable year 1922 or subsequent taxable years? ✓ If the answer to this question is "yes," these forms will not be required, except under the circumstances described in question (b). If the answer to this question is "no," and the answer to questions 4, 5, and 6, or to any of them, is "yes," procure from the Collector of Internal Revenue for your district Forms 851, 852, 853, and 853A, Affiliations Schedules 1, 2, 3, and 4, which shall be filled in and filed as a part of this return. If the answer to this question is "no," question (b) need not be answered.

(b) Did substantially the same conditions, as are set out in the Affiliations Schedules filed for 1926 or prior years, obtain during the entire taxable year 1927? Yes If the answer to this question is "no," a statement, setting forth the particulars in which the situation has changed, should be attached to and made a part of this return. If there have been substantial changes in stockholdings, a complete schedule of such changes should be submitted on Form 853, Affiliations Schedule 3. If there are companies other than those covered by the Affiliations Schedules for prior years which, applying the tests contained in questions 4, 5, or 6, may have come into the affiliated group since 1926, Forms 851, 852, 853, and 852A, are required for the entire group for the taxable year.

(c) Did the corporation file a consolidated return for the preceding taxable year? No

PREDECESSOR BUSINESS

8. Did the corporation file a return under the same name for the year preceding taxable year? Yes Was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or any prior year since December 31, 1917? ✓ If answer is "yes," give name and address of each predecessor business, and the date of the change in entity.

Upon such change were any asset values increased or decreased? ✓ If the answer is "yes," closing balance sheets of old business and opening balance sheets of new business must be furnished.

BASIS OF RETURN

9. Is this return made on the basis of actual receipts and disbursements? Yes If not, describe fully what other basis or method was used in computing net income. ✓

LIST OF ATTACHED SCHEDULES

10. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the taxpayer should be placed on each separate schedule accompanying the return. ✓

AFFIDAVIT

We, the undersigned, president and treasurer of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return made in good faith, for the taxable year as stated, pursuant to the Revenue Act of 1926 and the Regulations issued under authority thereof.

Sworn to and subscribed before me this 16th day of February, 1928

NOTARIAL SEAL

A. J. Nolan (Signature of officer administering oath), Notary Public (Title)

A. J. NOLAN
Notary Public St. Louis Co., Minn
My Commission Expires Jan. 30, 1935

CORPORATE SEAL

J. S. Washburn, President

Philip L. Ray, Treasurer, Secy

GOVERNMENT PRINTING OFFICE 2—14448

5858

Alworth-Washburn Co.
vs.
David Burnet Com. & c.

F333A

CARD NO.

Group 1 Class 112 Acct 51

LINE

NAME ALWORTH WASHBURN COMPANY

GUARANTY

ADDRESS DULUTH, MINNESOTA

REMINGTON RAND BUSINESS SERVICE INC.

22 LIBRARY BUREAU FORM 562-3679

Date 1927	NO.	MAKER OR ENDORSER	Rate	Class	Date Due	Date Paid	DEBIT	CREDIT	DIRECT LINE	COLLATERAL LINE	INDIRECT LINE	TOTAL LINE
12/6	79326	Brooks Scanlon Dr. Co. F.A.C.	5	C	5/1/28	5-1	25000 -					
	7	" " "	"	C	May 1 '30	5-1	23180 -					
	8	" " "	"	C	May 1 '31	5-1	25000 -					
	9	" " "	"	C	May 1 '31	5-1	25000 -					
	30	" " "	"	"	May 1 '31	5-1	25000 -					
	1	" " "	"	"	May 1 '31	5-1	23180 -					
	2	" " "	"	"	May 1 '28	5-1	25000 -					
	3	" " "	"	"	May 1 '28	5-1	25000 -					
	4	" " "	"	"	May 1 '28	5-1	23180 -					
	5	" " "	"	"	May 1 '29	5-1	25000 -					
	6	" " "	"	"	May 1 '29	5-1	25000 -					
	7	" " "	"	"	May 1 '29	5-1	25000 -					
	8	" " "	"	"	May 1 '29	5-1	23180 -					
	9	" " "	"	"	May 1 '30	5-1	25000 -					
	40	" " "	"	"	May 1 '30	5-1	25000 -					
	1	" " "	"	"	May 1 '30	5-1	25000 -			392720 -		392720 -
5/1		79326-79332-3-4-5						98180 -		294540 -		294540 -
5/1		793356-7-8						98180 -		196360 -		196360 -
1930 5/1		79327-39-40-1						98180 -		98180 -		98180 -
1931 5/1								98180 -		0		0

U. S. BOARD OF TAX APPEALS
DIV. 8 DOCKET 45651
ADMITTED IN EVIDENCE
JUN 14 1931
PETITIONER'S
EXHIBIT 8
~~RESPONDENT'S~~

82 U. S. Board of Tax Appeals, Div. 8.

Docket 45651.

RESPONDENT'S EXHIBIT B.

Admitted in Evidence Jun. 14, 1931.

Meeting of the Board of Directors.

Held Dec. 10, 1927.

The Board of Directors of Alworth-Washburn Company convened at the Company's office, #1600 Alworth Building, Duluth, Minnesota, on Saturday, December 10th, 1927, at ten o'clock A. M., pursuant to written consent and waiver of notice signed by all the existing directors of said company, which consent is as follows:

"We the undersigned, constituting all the member- of the Board of Directors of Alworth Washburn Company, hereby waive notice and consent to the holding of a meeting of said Board in the Company's office, 1600 Alworth Building, Duluth, Minnesota, at 10:00 A. M. on Saturday, the 10th day of December, 1927, for the following purposes:

(1) To confirm the sale of $392,720.00 of notes of the Brooks-Scanlon Lumber Company held by this company, representing deferred payments upon timber lands heretofore sold to said Brooks-Scanlon Lumber Company, which notes were recently sold by the executive officers of this Company for $403,882.93, and endorsed in the name of the Company with waiver of presentment for payment, protest, notice of protest and non-payment;

(2) To confirm the partial distribution of said funds to the stockholders of this company made by the executive officers on December 6, 1927;

(3) To consider the matter of tax obligations and the reservation of funds therefor;

(4) To authorize the execution of a deed or deeds for any of the properties heretofore sold by this Company to the said Brooks-Scanlon Lumber Company for which payment has not yet fully been made, and the depositing of such

deed or deeds in escrow with a responsible bank or trust company for delivery when the said purchasers shall be entitled thereto;

(5) To fill the vacancy existing on the Board of Directors of this Company.

Dated December 8, 1927.

J. L. WASHBURN.
M. W. ALWORTH.
R. D. ALWORTH.
W. D. BAILEY."

There were present directors M. W. Alworth, W. D. Bailey and J. L. Washburn. The President of the corporation presided at the meeting and the Secretary acted as recording officer.

83 Upon motion of Director M. W. Alworth, seconded by Director Bailey, the minutes of the last meeting of the Board of Directors were approved as recorded. It appearing that Mr. M. H. Alworth, formerly a Director of this Company, had some time since disposed of and transferred all of his stock in the corporation, and that under the Articles of Incorporation directors are required to be stockholders, upon motion of Director M. W. Alworth, seconded by Director Bailey, it was voted that the office of director heretofore held by Mr. M. H. Alworth be declared vacant and that Mr. Philip L. Ray, the secretary of the corporation, be elected director to fill such vacancy.

Mr. Ray was present and signified his acceptance of the office and thenceforth participated in the proceedings of the meeting.

The President reported that acting by concurrence of the principal stockholders, he and the Treasurer had authorized the Secretary, Mr. Philip L. Ray, to consummate a sale of all of the notes held by this Company against Brooks-Scanlon Lumber Company of Minneapolis, Minnesota, accrued from the sale of its timber lands in Jefferson County, Oregon, by contract of sale dated May 1, 1926. That the first series of notes described in said contract, aggregating $98,180.00, due May 1, 1927, were promptly paid, the remaining notes numbered 5 to 20, inclusive, aggregating $392,720.00 principal and maturing in series aggregating $98,180.00 in principal on May 1, 1928, 1929, 1930 and 1931, respectively, all of said notes bearing even date

with said contract and bearing 5% interest payable annually. That the Secretary pursuant to said authority consummated such sale to the First National Bank of Minneapolis for the sum of $403,882.93, and that the President and Secretary had endorsed the said notes in the name and behalf of this company with waiver of presentment for payment, protest, notice of protest and non-payment, delivered the notes and received through the Secretary payment therefor. That the same had been deposited in the Northern National Bank to the Company's credit and that $350,000.00 thereof had been distributed upon the checks of the Treasurer, countersigned by the President, to the stockholders of the Company, being at the rate of $70.00 per share, the residue of the money still remaining to the Company's credit in its bank of deposit. That in the remittance of such funds to the stockholders, the President had advised each stockholder that in the near future the Company's expert tax accountant would make a calculation with reference to what portion thereof should be treated as income, and that the stockholders would be duly advised of his conclusion.

Whereupon upon motion of Director Bailey, seconded by Director M. W. Alworth, the actions thus reported by the President were in all respects ratified, approved and confirmed.

The President and Secretary further reported that the chairman of the Executive Committee of the First
84 National Bank of Minneapolis had asked the conveyance of the property sold under the said contract to Brooks-Scanlon Lumber Company, out of which the said notes arose, should be made by this company to the Brooks-Scanlon Lumber Company and deposited in escrow with said Bank for delivery when the remainder of said notes should be paid or taken up.

Whereupon, upon motion of Director M. W. Alworth, seconded by Director Ray, the President and Secretary were authorized to execute such deed in accordance with the said contract for the property therein described, and deliver the same to the First National Bank of Minneapolis to be held in escrow until the said notes representing all of the balance of the unpaid purchase price set forth in said contract be paid or taken up.

The Treasurer stated that he could not at this time definitely advise how much money would be required for the discharge of all the tax obligations of this company to the Federal Government, but upon consultation with the Company's tax expert and accountant he had concluded that all of the company's funds in excess of $350,000.00 had best be held until adjustments are completed and the tax obligations are discharged.

Upon motion of Director Bailey, seconded by Director Ray, this conclusion was concurred in and the President and Treasurer were authorized to keep such funds in the Company's bank of deposit in such form as would render the same available when required and as will in their judgment best subserve the Company's interests.

It appearing that all the notes representing the deferred payments of consideration for the sale of this Company's lands in Deschutes County, Oregon, made to the Brooks-Scanlon Lumber Company of Minneapolis, Minnesota, by contract dated October 1, 1923, except the series aggregating $187,820.34, due January 15, 1928, and a like amount due January 15, 1929, had been duly and promptly paid, and that after the payment of the next maturing series, the First National Bank of Duluth, Minnesota, will be the holder of all the remaining unpaid notes, upon motion of Director M. W. Alworth, seconded by Director Ray, it was voted that the President and Secretary be hereby authorized to duly execute in the name and under the corporate seal of this company deed for said property in accordance with the terms of said contract to the said Brooks-Scanlon Lumber Company and to deliver the same upon the payment of the residue of said notes, or if requested by the First National Bank of Duluth to execute such deed and deposit the same in escrow with said Bank for delivery to the said Brooks-Scanlon Lumber Company when all of said notes should be paid or taken up.

There being no further business to come before the meeting, upon motion of Director Ray, duly seconded, the same was adjourned.

(Sgd.) J. L. WASHBURN,
President.

(Sgd.) PHILIP L. RAY,
Secretary.

85 [Stamp:] United States Board of Tax Appeals. Filed Oct. 28, 1932.

United States Board of Tax Appeals.

B. T. A. Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Præcipe for Record.

To the Clerk of the United States Board of Tax Appeals:

You are hereby requested to prepare and certify and transmit to the Clerk of the United States Court of Appeals of the District of Columbia, with reference to the petition for review heretofore filed by the petitioner in the above cause, a transcript of the record in the above cause, prepared and transmitted as required by law and by the rules of said Court, and to include in said transcript of record the following documents or certified copies thereof:

1. The docket entries of proceedings before the United States Board of Tax Appeals in the above entitled cause.
2. Pleadings before the Board.
3. Opinion and decision of the Board.
4. Petition for Review.

86 5. The statement of evidence (including exhibits), as settled or agreed upon.

6. Stipulation for review by Court of Appeals of the District of Columbia.
7. This præcipe.

M. P. WORMHOUDT,
Attorney for Petitioner.

87 United States Board of Tax Appeals, Washington.

Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Certificate.

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 86, inclu-

sive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Præcipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 22nd day of November, 1932.

[Seal U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk United States Board of Tax Appeals.

88 United States Board of Tax Appeals.

Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Order Enlarging Time.

On motion of counsel for the petitioner and consent of counsel for the respondent, it is

Ordered that the time for preparation of the evidence and transmission and delivery of the record *sur* petition for review of the above entitled proceeding in the Court of Appeals for the District of Columbia, be and it is hereby extended to November 14, 1932.

(Signed) ERNEST H. VAN FOSSAN,
Member.

Dated Washington, D. C., Aug. 26, 1932.

jd.

A true copy.

[Seal U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clk.

89 United States Board of Tax Appeals.

Docket No. 45651.

ALWORTH-WASHBURN COMPANY, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Order Enlarging Time.

For cause appearing of record, it is

Ordered that the time for filing certified copies of record papers *sur* petition for review of the above entitled proceeding in the Court of Appeals of the District of Columbia be and it is hereby extended to December 1, 1932.

(Signed) LOGAN MORRIS,
Member.

Dated Washington, D. C., November 14, 1932.

A true copy.

[Seal U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clk.

Endorsed on cover: Board of Tax Appeals. No. 5858. Alworth-Washburn Company, appellant, vs. David Burnet, Commissioner of Internal Revenue. Court of Appeals, District of Columbia. Filed Nov. 26, 1932. Henry W. Hodges, Clerk.

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FOR MR. CHIEF JUSTICE MARTIN

COURT OF APPEALS
DISTRICT OF COLUMBIA
FILED
MAR 3 - 1933
Henry W. Hodges
CLERK

IN THE

Court of Appeals, District of Columbia

No. 5858.

309

ALWORTH-WASHBURN COMPANY, *Appellant*,

vs.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE.

APPEAL FROM THE UNITED STATES BOARD OF TAX APPEALS.

BRIEF FOR APPELLANT.

PAUL E. SHORB,
M. P. WORMHOUDT,
Attorneys for Appellant.

COVINGTON, BURLING & RUBLEE,
Of Counsel.

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THE ASSOCIATION OF THE BAR
OF THE CITY OF NEW YORK

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Kester Accounting Theory and Practice, Vol. 1, p. 322 25
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IN THE

Court of Appeals, District of Columbia

No. 5858.

ALWORTH-WASHBURN COMPANY, *Appellant*,

vs.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE.

APPEAL FROM THE UNITED STATES BOARD OF TAX APPEALS.

BRIEF FOR APPELLANT.

Jurisdiction.

This case comes before the Court on petition for review of a decision of the United States Board of Tax Appeals pursuant to Sections 1001, 1002 and 1003 of the Revenue Act of 1926. In the stipulation filed in the case (Record page 11), it was agreed that the case might be reviewed by the Court of Appeals of the District of Columbia pursuant to the provisions of Section 1002 (d) of said Act (44 Stat. L. 9, 109, 110).

The Question Presented.

This case involves the taxable year 1927. In 1926 the appellant sold its property receiving less than twenty-five per cent in cash and the balance in installment notes. The profit from the transaction was reported on the installment basis in appellant's 1926 return. In 1927 the installment notes remaining were discounted by appellant with unqualified endorsements. The appellant reported the profit reflected in these notes in its returns for the subsequent years when the maker actually paid them. The Board of Tax Appeals held that the profit reflected in the notes was income to the appellant in the year 1927.

The only question in this case is whether the profit reflected in these installment notes was income to the appellant in 1927 or in the subsequent years in which it was reported by appellant.

Statement of Facts.

The Alworth-Washburn Company is a Minnesota corporation with its principal office at Duluth, Minnesota, (R. 3, 7).

The purpose of the company in acquiring timber was to hold it *en bloc*, to sell it rather than to operate it, and to make a block sale at the earliest possible moment, (R. 18). In May, 1926, the appellant sold the remainder of its timber assets (R. 22) to the Brooks-Scanlon Lumber Company for $588,838.02, (R. 17).

Of the purchase price $100,000.00 was paid in cash and the remainder was evidenced by five notes of the Brooks-Scanlon Lumber Company, due May 1, of each of the years 1927, 1928, 1929, 1930 and 1931, (R. 27).

Upon payment of the whole purchase price the Alworth-Washburn Company agreed to execute and deliver to Brooks-Scanlon Lumber Company, a warranty deed covering the timber lands and premises so sold and located in Jefferson County, State of Oregon (R. 26, 28).

In its 1926 federal tax return the appellant reported the income from the transaction on the installment basis, which basis was accepted by the Commissioner of Internal Revenue for that year, (R. 34, 35, 49, 54, 55).

On December 6, 1927, the First National Bank of Minneapolis, Minnesota, (hereafter referred to as the bank) discounted for the appellant, the remaining Brooks-Scanlon Lumber Company installment notes aggregating $392,720.00, (R. 19). The notes were unqualifiedly endorsed by the appellant, the appellant waiving presentment for payment, protest, notice of protest and non-payment of the notes (R. 47).

The bank kept their record of the transaction on a liability ledger card, bearing the name of Alworth-Washburn Company (R. 18, 81). The total of all cards of this type would show bills discounted by the First National Bank of Minneapolis, which in banking parlance means the same thing as loans made. The aggregate of the footings on these cards would show the bank's total loans and discounts. (R. 19)

The "collateral" record of the bank showed that the bank received the warranty deed to the timber land sold by the Alworth-Washburn Company, as collateral in connection with this loan (R. 20). The liability ledger card would have been headed the same way if the Alworth-Washburn Company had given the bank its note and the Brooks-Scanlon notes as collateral. So

far as the bank was concerned the transaction would be identical and it would have made no different decision in the acceptance of this paper. If the notes had not been paid the bank would have looked to the Alworth-Washburn Company for payment. (R. 20)

During this period the bank had a line of credit extended to the Brooks-Scanlon Lumber Company but these installment notes were not applied against that line of credit. They would have been permitted their entire line of credit in addition to any of their obligations on these notes. (R. 20)

The bank's statement of assets and liabilities to the bank examiner shows loans and discounts as an asset, which indicated the amount of money the bank had loaned direct to customers and discounted paper for them (R. 20). These Brooks-Scanlon notes which required the endorsement of Alworth-Washburn Company were included in that statement of assets under that head. The account of the Alworth-Washburn Company represented by the liability ledger card, (R. 81) was a component part of the bank's assets headed loans and discounts. (R. 21)

The Alworth-Washburn Company could have made arrangements with the bank to take these notes if agreeable to the bank. The bank was under no obligation to return the notes to the appellant and accept money before maturity but the appellant might have concluded a transaction by which it paid the bank the money and secured the return of the notes. (R. 21) In the case of any default whatever the bank would have immediately demanded that the Alworth-Washburn Company pay it for the notes (R. 21, 22). The bank would not have proceeded against the Brooks-Scanlon Company (R. 22).

Had the bank been willing and taken these notes from Alworth-Washburn Company without recourse, it would have made an entirely different entry on its books (R. 22). In that case the amount of indebtedness would have been added to other indebtedness of Brooks-Scanlon Company in determining whether their line of credit was exhausted (R. 22). The bank did not purchase notes of their customers who had lines of credit although it frequently discounted them for other people (R. 22). Purchase of such paper was considered by the bank as unfair to its customers since it immediately upset the credit of the customer (R. 22). The bank did buy paper on the open market from brokers on which there is no recourse whatever against the sellers of the paper and in such cases the bank looks to the maker of the paper (R. 22).

The minutes of the meeting of the directors of the Alworth-Washburn Company held December 10, 1927, referred to the transfer of the Brooks-Scanlon Lumber Company notes to the bank as a sale thereof (R. 38, 39). The minutes also provided that the officers were authorized to execute a deed to the timber land sold to the Brooks-Scanlon Company and that the deed be delivered to the bank to be held in escrow until the notes representing all of the balance of the purchase price be paid or taken up (R. 39).

After the sale of the timber lands in 1926 the only asset of the company other than the Brooks-Scanlon notes was cash retained in bank (R. 23). After being discounted, the notes in the amount of the unpaid balances thereon, were carried on the books, financial statements to banks and income tax returns as liabilities through 1931. The corresponding asset has been carried on the asset side or notes receivable. (R. 23)

The cash received from the discount of the notes was distributed to the company's stockholders, except a sum considered sufficient to take care of income tax obligations and other obligations of the company (R. 24). The distributions to the stockholders were charged as advances to them on the company's books and as an asset of the company (R. 24). The amounts turned over to the stockholders were charged to them because they would have to pay the money back if the maker of the notes defaulted (R. 24).

Subsequent to the year 1927, the average operating expenses of the company totalled about $1,500 per year, made up of license fees to certain states and audit expenses (R. 23). The functions performed by the corporation during these years were to inquire from time to time as to the payment of the notes of the makers and to prepare income tax returns to the Federal Government and the States of Oregon and Minnesota (R. 24).

The notes were in each instance paid on their due date (R. 24). The appellant has reported all of the income reflected in said notes in its federal income tax returns for the years in which the maker paid said notes (R. 49 to 80, incl.).

On these facts the appellant contended before the Board of Tax Appeals that it realized no taxable income in the year 1927 from discounting, with unqualified endorsement, the Brooks-Scanlon Company notes with the First National Bank of Minneapolis. The Board held that the profit reflected in said notes was realized and taxable as part of taxpayer's income for the year 1927.

From this decision the Alworth-Washburn Company has brought this case before this Court on Petition for Review.

Assignments of Error.

The following errors have been assigned:

The Board erred:

1. In entering judgment for respondent.

2. In failing to enter judgment for petitioner.

3. In redetermining the deficiency as $19,005.60 for the year 1927.

4. In holding and deciding that the discounting of notes constitutes a sale of notes instead of a loan by the discounting bank.

5. In holding and deciding that the installment sale of petitioner's timber became a closed transaction on December 6, 1927, when petitioner discounted the Brooks-Scanlon Lumber Company notes with the First National Bank of Minneapolis.

6. In holding and deciding that the taxable profit on the sale of petitioner's timber to Brooks-Scanlon Lumber Company could be determined in the year 1927.

7. In holding and deciding that petitioner actually received "payments" when it discounted the Brooks-Scanlon Lumber Company notes in 1927.

8. In failing to hold and decide that proper and approved standard methods of accounting did not permit the determination of any profit when petitioner discounted said Brooks-Scanlon Lumber Company notes to the First National Bank of Minneapolis.

9. In finding and holding that the petitioner sold the Brooks-Scanlon Lumber Company notes to the First National Bank of Minneapolis on December 6, 1927, because such finding is not supported by and is contrary to the evidence adduced at the hearing before the Board.

10. In finding and holding that the transaction between petitioner and the First National Bank of Minneapolis, to which it endorsed said Brooks-Scanlon Lumber Company notes, did not constitute the loan of money by said bank to the petitioner with the notes transferred as collateral, because said finding is not supported by and is contrary to the evidence adduced at the hearing before the Board.

11. In holding and deciding that the petitioner realized taxable income in 1927 from its transfer of Brooks-Scanlon Lumber Company notes to the First National Bank of Minneapolis.

12. In failing to find and hold that the transaction between the petitioner and the First National Bank of Minneapolis, to which it endorsed the Brooks-Scanlon Lumber Company notes, constituted the loaning of money by said bank to the petitioner with the notes transferred as collateral, as was established by the evidence adduced at the hearing held before the Board.

13. In failing to hold and decide that the petitioner realized no taxable income from its transfer of the Brooks-Scanlon Lumber Company notes to the First National Bank of Minneapolis in 1927.

14. In failing to hold and decide that the petitioner correctly reported the profit represented in said Brooks-Scanlon Lumber Company notes in the years subsequent to 1927, when said Lumber Company actually paid said notes.

ARGUMENT.

The Statute Involved.

The right of the Alworth-Washburn Company to defer the profit reflected in the notes of the Brooks-Scanlon Lumber Company until the year the notes are paid, arises out of Section 212 (d), Revenue Act of 1926 (44 Stat. L. 23) which is as follows:

> "Under regulations prescribed by the Commissioner with the approval of the Secretary, a person who regularly sells or otherwise disposes of personal property on the installment plan may return as income therefrom in any taxable year that proportion of the installment payments actually received in that year which the total profit realized or to be realized when the payment is completed, bears to the total contract price. In the case (1) of a casual sale or other casual disposition of personal property for a price exceeding $1,000, or (2) of a sale or other disposition of real property, if in either case the initial payments do not exceed one-fourth of the purchase price, the income may, under regulations prescribed by the Commissioner with the approval of the Secretary, be returned on the basis and in the manner above prescribed in this subdivision. As used in this subdivision the term 'initial payments' means the payments received in cash or property other than evidences of indebtedness of the purchaser during the taxable period in which the sale or other disposition is made."

Basis of the Board's Decision.

The Board of Tax Appeals in its decision referred to the cases of *Grace T. Mytinger,* 4 B. T. A. 896, *Packard Cleveland Motor Company,* 14 B. T. A. 118 and *Lucius H. Elmer,* 22 B. T. A. 224, as authority for its decision.

The appellant submits that the issue and the material facts involved in each of those cases are sufficiently different to justify the conclusion that they are not applicable to the present case. But even though the facts and issues could be considered as similar or identical to those in the present case, the appellant contends that the decisions by the Board of Tax Appeals in those cases are erroneous.

In each of the aforementioned decisions the question involved the right of the taxpayer to report the profit from a sale on the installment basis. That right is not disputed in the present case. In each of the foregoing cases, the notes taken as part of the sale price were disposed of from year to year in the regular course of business and the taxpayers continued to carry on their regular business with its resulting yearly current income. In the present case the corporation continued its existence solely because of its liability on the notes discounted. Finally in the decisions relied upon by the Board, there was no evidence presented as in the present case which definitely established that the discount of notes was in fact a loan of money by the bank to the taxpayer.

The Court's attention is invited to the fact that the Lucius H. Elmer case is now before the Circuit Court of Appeals, Second Circuit on Petition for Review by the taxpayer. The Packard Cleveland Motor Car Com-

pany case was not appealed, apparently because subsequent to the Board's opinion in that case, the Board revised its decision and eliminated most of the deficiency, the statute of limitations being applicable under the decision of *Russell v. United States*, 278 U. S. 181.

The Packard Cleveland Motor decision is commented on as follows in Roberts Manual to United States Board of Tax Appeals Reports, Part II, page 1584:

> "The decision on the merits seems erroneous, because the so-called 'sale' of notes seems actually to have been disguised borrowings on the security of such notes as collateral."

The Brooks-Scanlon Notes Being Unqualifiedly Endorsed by Alworth-Washburn Company, Eliminates Any Possibility That a Sale of Said Notes Occurred.

It is quite obvious that if the appellant had divested itself of the notes in question by an outright sale thereof without any recourse on itself or had the notes been paid by the maker in 1927, the profit reflected in said notes would be income in 1927.

It is undisputed that the maker did not pay the notes in 1927 so the possibility of income on that basis is eliminated. Consideration of a single fact present in this case and the law applicable thereto definitely establishes there was no "sale" of the notes.

The record shows (R. 18, 23) and the Board's opinion states (R. 9) that the appellant discounted the notes to The First National Bank of Minneapolis. The record also shows (R. 47) that the back of each note

contained the following endorsement of Alworth-Washburn Company:

> "The endorser hereof waives presentment for payment, protest, notice of protest and non-payment of this note."

On the basis of this endorsement alone the appellant submits that the Board erred in holding that discounting the notes constituted a "sale" instead of a "loan". Had the appellant endorsed the notes without recourse or simply assigned the notes without incurring any liability for their payment the result might have been different, but in this case it is undisputed that Alworth-Washburn Company in the year 1927 did not and could not know the amount of profit it would realize on these notes. It is true that it had been advanced money on the notes but its corresponding liability to make good the payment of the notes remained until the last note was paid by the maker.

The position of the appellant is supported by a respectable line of decisions which involved the interpretation of usury laws and thus required a definite decision on whether a transaction constituted a sale or a loan. A leading case on the subject is *Bynum v. Rogers,* 49 North Carolina Reports 399. In that case the Court, after citing *Collier v. Nevill,* 14 N. C. 30, *McElwee v. Collins,* 20 N. C. Reports, 209 and *Ballinger v. Edwards,* 39 N. C. Reports, 449 said (page 401):

> "These cases establish a clear rule by which to distinguish between a sale of a bill or note and a loan, to wit, *when the instrument is transferred by the endorsement of the person receiving the*

> *money, it is a loan, because the endorser is liable for the debt;* but when the transfer is simply by delivery, it is a sale, if the transaction is bonafide." (Italics ours)

In the case of *McElwee v. Collins,* 20 N. C. Reports, 209, 210, the Court said:

> "There is a distinction between taking a bill, and advancing money on it, with an endorsement or guaranty, and one without it. The last is a *purchase* and may be for less than the real value; the other is a loan and is within the operation of the Statute of Usury."

The principle of law stated in the aforementioned cases has been followed in the recent cases of *Pratt v. Mortgage Company,* 196 N. C. 294, 298 and *Sedbury v. Duffy,* 158 N. C. 432. In the former case, the Court said (page 298):

> "As between the maker and the assignee or endorsee there is no usurious transaction, which is subject to the statutory penalties. It is otherwise, however, as between the endorsee and endorser, who becomes liable by his endorsement for the amount due on the note. As between them the transaction is a loan of money, and if more than six per cent per annum is knowingly charged, the transaction is usurious."

The same rule has been applied by the Courts of the State of Wisconsin. In the case of *Cowles v. McVickar,* 3 Wisconsin, 637, 643, the Court said:

> "A note or bill may be sold in the market for less than its value, and the payee may endorse the note so as to pass the title. Such a transaction

would not necessarily be usurious. But the endorser in such a case would not be liable for the payment of the note. This transaction would be a sale, nothing more nor less and the endorsee might, if the endorsement were in blank, fill it up without recourse and recover of the maker. *But where a note is transferred by the payee, and endorsed by him in the usual manner, or the payment guaranteed by him, in consideration of a certain sum paid or advanced by the endorsee, the transaction is essentially a loan. It is the same as though the endorser or guarantor had given his own note. He becomes liable for the repayment of money at all events.* If I raise money by the sale of a horse, I do not become liable for the repayment of the money. So if I raise money by the sale of a note. But if I raise money by giving my own note for its repayment or the note of another person and guarantee its payment, the transaction is a loan." (Italics ours)

In the subsequent case of *Rock County Bank v. Wooliscroft,* 16 Wisconsin, 22, 28, it is stated:

> "But when the note is endorsed by the payee in the usual manner, in consideration of a sum paid or advanced by the endorsee, the transaction is essentially a loan, and exacting a higher premium than the legal rate of interest, renders the contract void for usury."

The Courts of Kentucky have also recognized the significance of an unqualified endorsement in the case of *Newell v. First National Bank of Somerset,* 13 Kentucky Law Reporter, 775, 776, where the Court said:

> "The word discount denotes the act of giving money for a bill of exchange or promissory note, deducting the interest. As distinguished from dis-

> counting, the word buying is used when the seller does not endorse the note, and is not accountable for its payment."

The question of whether the transfer of a note with full endorsement was a sale thereof or simply a loan by the bank to the endorsee arose in the case of *First National Bank of Greenville v. Sherburne,* 14 Ill. App. 566. The evidence disclosed that the note was endorsed in blank by the payee and before maturity delivered to and taken by the bank in the usual course of business. The Court held that the fair and reasonable presumption from the fact that the note was taken in the "usual course of business" of a national bank would be that it was discounted; that although in form and common parlance it was a purchase of the note, yet in substance it was a loan by way of discount made by the bank to the payee and the relation of debtor and creditor as between them was created. The Court said (page 570):

> "Had the transfer been by delivery only, or by an endorsement without recourse, then, probably it might be regarded as an absolute purchase of the note. * * * *If the party dealing with the bank assumes a responsibility it is a loan; if he does not it is an advance made to him in consideration of the transfer without recourse or by delivery."* (Italics ours)

The Supreme Court of the United States has also indicated that a transfer of a note by endorsement with full recourse on the endorser establishes the transaction to be a loan. In the case of *National Bank v. Johnson,* 104 U. S. 271, the question arose whether a national bank was guilty of violating the usury laws in

discounting notes at 12 per cent per annum—the notes being transferred by endorsement. The Supreme Court affirmed the judgment of the lower Court which had found the bank guilty of violating the usury statutes. The Supreme Court said (page 278):

> "In the present case, the paper was transferred by an endorsement imposing the ordinary liability upon the endorser. It may, perhaps, be distinguished from cases where the title to the paper is transferred by an endorsement without recourse, or by mere delivery. The advance in such cases, to the previous holder, of the agreed consideration can hardly be considered a loan, for the relation of debtor and creditor as between them is not created by the transaction, if made, as supposed, in good faith and not as a cover for usury."

Finally the Courts of Minnesota have spoken on the subject in no uncertain language. In the case of *Farmers etc. Bank v. Baldwin,* 23 Minnesota 198, 206, the Court said:

> "Discounting a note and buying it are not identical in meaning, the latter expression being used to denote the transaction when the seller *does not endorse the note* and is not accountable for it; (1 Bouv. Law Dict. title *Discount,* citing Pothier De l'Usure, 128) and it is admitted that such was the character of the transaction in this case. In view of this understanding of the functions of a bank of discount, the legal signification attached to the word 'discount' and the distinction between it and the word 'purchase' when applied to the business of banking, it is obvious that the power 'to carry on the business of banking, by discounting notes, bills and other evidences of debt' is only an authority *to loan money* thereon, with the right to deduct the legal rate of interest in advance." (Italics ours)

It is submitted that the rule of law laid down in the foregoing cases is sound. It is recognized by the Court in the Minnesota case cited above. The bank and the appellant in this case are both located in the State of Minnesota and the transaction in question was entirely consummated in that state. The present case is therefore governed by the foregoing decisions.

Alworth-Washburn Company discounted the Brooks-Scanlon notes with the First National Bank of Minneapolis. The transfer was not by mere delivery only or by endorsement without recourse. The endorsement on the contrary was with full recourse on the Alworth-Washburn Company and it assumed a definite liability for the payment of the notes. Accordingly under the law enunciated in the foregoing cases, a sale of the notes was not consummated but the transaction was essentially a loan.

The Board of Tax Appeals accordingly erred as a matter of law in holding to the contrary and in ruling that income was realized in 1927, when the notes were discounted with full recourse on the appellant.

The Decision of the Board is not Supported by Substantial Evidence.

As stated heretofore the Board of Tax Appeals erred as a matter of law in holding that the discount of notes with full recourse on the endorser constituted a sale of the notes and that income resulted therefrom to the endorser. But even if this error of law could be overlooked and the question is to be decided on the facts in the record it is submitted that there is no substantial evidence to support the Board's decision that

the discounting of the notes resulted in a sale thereof instead of a loan based on the notes.

The Board has stressed the fact that the minutes of the directors meeting of the Alworth-Washburn Company referred to the transaction as a sale. That the minutes in question are not substantial evidence to establish a sale is evident when it is remembered that (1) a transaction called a sale may in fact be a loan or pledge, and (2) even had the directors of the Alworth-Washburn Company intended the transaction to be a sale, it does not follow that a sale was actually consummated.

There is nothing sacred or conclusive about the use of the word "sale" in the minutes of the directors meeting. The label, name or the form does not determine the nature of the transaction. In the case of *J. W. Solof,* 1 B. T. A. 776, the contract between the parties stated that there was a *sale* of stock by the taxpayer. The taxpayer contended the transaction was in fact a mere loan of money. The Board properly held:

> "that the transaction while in form a sale was in reality a loan to the taxpayer, and the amount received did not constitute income."

Likewise this Court in the case of *Johnson Locke Mercantile Company v. Burnet,* 60 App. D. C. 272, held that the mere fact that parties called and labeled certain payments "interest" did not make them "interest" when they were actually payments of principal sums. Numerous cases could be cited in which parties called transactions sales and the Courts held they were in fact loans or pledges. See *Barker Piano Company v. Commercial Security Company,* 93 Conn. 129, 105 Atl. 328; *Dorothy v. Commonwealth Commercial Com-*

pany, 198 Ill. App. 601, 116 N. E. 143 and *Petition of National Discount Company,* 272 Fed. 570, 573, 575.

Moreover even though it could be shown that the directors of the Alworth-Washburn Company were ratifying a sale of the notes without further liability on the part of the company this would not decide the case. The Board of Tax Appeals should have determined what was actually done. As stated by the Supreme Court in *Weiss v. Stern,* 265 U. S. 242, 254:

> "Questions of taxation must be determined by viewing what was actually done, rather than the declared purpose of the participants; and when applying the provisions of the Sixteenth Amendment and income laws enacted thereunder we must regard matters of substance and not mere form."

The Board has sought to sustain its decision by referring to the fact that the money received by the taxpayer was distributed to its stockholders and furthermore that an official of the discounting bank had testified:

> "We were under no obligation to return the notes to them and accept money before maturity * * *." (R. 10)

The Board, however, failed to state that the same officer's testimony continued (R. 21):

> "but they might have concluded a transaction by which they could pay us money and return the notes to them" and "the Alworth-Washburn Company could have made arrangements with us to take these notes if agreeable to us."

Likewise the Board ignored the fact that the distributions were charged as advances to stockholders and that (R. 20):

> "They charged the amount turned over to the stockholders themselves because they would have to pay that money back if the makers of these notes had defaulted."

In the final analysis the evidence cited by the Board proves nothing and is quite immaterial. The mere fact that a company distributed the money secured on discounted notes does not establish a sale of the notes or a closed transaction. There was no valid reason why this money had to be kept in the treasury of the company, whether the transaction be a loan or a sale. The company could have used the money to acquire additional timber but such action would not have established a sale of the notes.

Assuming the bank was under no obligation to return the notes and accept money before maturity, does such fact establish a sale? Does not the same situation exist in every case where a company borrows money from the bank on its own note which is due on a definite later date? In the case of *every loan* the lender is not obligated to return the notes and accept money before maturity of the notes. Certainly these facts are not substantial evidence justifying a finding that a sale of the notes was made.

The Board of Tax Appeals in its opinion admits that the appellant "discounted the remainder of the installment notes" but it then disregards all of the evidence which overwhelmingly establishes that no sale in fact occurred and that both the bank and the tax-

payer treated the transaction as a mere advance of money on the notes.

In no portion of the testimony of Mr. Pomeroy, Vice-President of the First National Bank in Minneapolis is the word "sale" found. The witness invariably referred to the transaction as a discount of the notes and specifically states that bills and notes discounted means the same thing as *loans made* (R. 19). The card record of the bank recording the transaction was called the "liability ledger card" (R. 18) of the Alworth-Washburn Company of Duluth, Minnesota. The aggregate of such cards would show, not the total of paper owned and purchased by the bank, but the total "loans and discounts" (R. 19) of the bank. The bank required and received in connection with "this loan" collateral consisting of a deed to the timber land (R. 20). Certainly this would not have been required in the case of an outright sale of notes. The witness, however, specifically refers to the transaction as "this loan."

The record further shows (page 20) that had the Alworth-Washburn Company, instead of tendering the Brooks-Scanlon Company notes for discount, borrowed money from the bank upon their note and deposited the Brooks-Scanlon notes as collateral to their loan the transaction would have been identical in so far as the bank was concerned. Furthermore, the Brooks-Scanlon notes were not applied by the bank against that company's line of credit (R. 20) as would have been the case if the bank had purchased the notes (R. 22). Had the bank been willing to and had taken the Brooks-Scanlon notes *without recourse* the transaction would have been entered on their books in an entirely different manner. In that case the amount of

the indebtedness would have been added to the other indebtedness of the Brooks-Scanlon Company (R. 22). The bank in fact did not *purchase* notes of their customers of which Brooks-Scanlon Lumber Company was one (R 22). The bank did buy paper on the open market from brokers on which there is no recourse at all upon the sellers of the paper (R. 22). This testimony unequivocally negatives any possibility that the bank in fact purchased the notes of Brooks-Scanlon Lumber Company. Stronger language could not have been used by the witness.

Adding to the conclusive and uncontroverted testimony on this point the witness stated (R. 21): "these Brooks-Scanlon notes that required endorsement would be included in the statement of assets under that head", namely "loans and discounts." Again the distinct liability of the Alworth-Washburn Company is emphasized on page 21 of the record. The witness on cross-examination was asked what the bank would have done had the makers of the notes failed to pay and the bank could not have realized the proceeds from the loan. He replied:

> "We would not have done anything with the loan. If the Brooks-Scanlon Company had not paid the notes we would have notified the Alworth-Washburn Company and asked them to take them up."

Continuing on re-direct examination the witness said (R. 21):

> "In the case of any default whatever we would have immediately demanded that the Alworth-Washburn Company pay us for the notes. We

> would not have proceeded against Brooks-Scanlon Company."

The foregoing is what the evidence shows actually happened in this case. To hold that the bank purchased the notes of the Brooks-Scanlon Company from the Alworth-Washburn Company is to ignore the undisputed evidence in this case and still that is the effect of the decision of the Board of Tax Appeals. Not only is the Board's decision unsupported by any substantial evidence but it is contrary to all the material evidence in this case.

The conduct and acts of the appellant are in accord with the treatment of the transaction by the bank. The discounted notes in the amount of unpaid balances thereon were carried as liabilities on the company's books, income tax returns and statements made to banks. See Record page 23 and balance sheets attached to income tax returns (R. 65, 69, 73, 77). All of said returns were sworn to by the president and secretary of the Alworth-Washburn Company and must have represented the intent and understanding of the corporation with respect to the transaction.

Finally the use of the word "discount" in describing the transaction (used by the Board in its opinion and by the witness Pomeroy no less than fifteen times in his testimony) must be presumed to have been used in its well accepted sense. As stated in *Weckler v. First National Bank,* 42 Maryland 581, 592:

> "The ordinary meaning of the term 'to discount' is to take interest in advance and in banking is a mode of loaning money."

In the case of *National Bank v. Johnson,* 104 U. S. 271, 277, it is stated:

> "So that the discount of negotiable paper is the form according to which they (national banks) are authorized to make their loans, and the terms 'loans' and 'discounts' are synonyms. It was so said in *Talmage v. Pell* (7 N. Y. 328); and in *Niagara County Bank v. Baker* (15 Ohio St. 68) the very point decided was that 'to discount paper, as understood in the business of banking, is only a mode of loaning money with the right to take the interest allowed by law in advance'."

The appellant realizes that the power to discount may include the power to purchase by discount but submits that the ordinary meaning of the term simply contemplates a loan of money. That the notes in this case were "discounted" is not contradicted and the Board so found. That the word should be used in its well accepted sense is logical and reasonable. That it was used in this case to indicate a loan and not a purchase is conclusively established by all of the evidence in the case.

The Court of Appeals should accordingly hold that the decision of the Board is not supported by any substantial evidence, but on the other hand is contrary to all of the material evidence in the case.

The Decision of the Board is Contrary to all Sound Methods of Accounting.

Testing the decision of the Board of Tax Appeals in the light of sound accounting methods, reveals another reason for holding that the Board erred in its decision in this case.

Sound accounting principles usually govern decisions in these tax problems, especially so when they are not in conflict with the law, so in preparing appellant's return for 1927 and subsequent years recourse was had to many text books of accounting authorities, including methods of accounting prescribed by the Federal Reserve Board, and it was found that practically every one of them laid down rules which, if followed, would not permit of the determination of any profit *as a result of* the discounting of the notes. In other words, the liability of appellant created by its unqualified endorsement of the notes had to be carried and reflected in its books. This being so, the proceeds of the notes when discounted had to be credited to a liability account, under some such caption as "Notes Receivable Discounted" and could not properly be credited to sales or profit and loss, and, if the money realized on the notes was not a proper credit to profit and loss, then there was no profit incident to the transaction, unless a further book entry, groundless and taken from no-where, be indulged in whereby installment sales might be debited and completed sales credited with the amount realized.

Kester, in his Accounting Theory and Practice, Vol. 1, Chapter XXXVIII, pp. 322-325, after setting up, in skeleton form, the proper journal entry for recording notes receivable discounted—viz:

Cash,	Dr.
Interest and Discount,	Dr.
To Notes Receivable Discounted,	Cr.

Says:

> "The practice of cancelling the liability against the corresponding asset and by a feat of mental

dexterity persuading oneself that there is therefore no need to show the item on the balance sheet, is a practice to be universally condemned."

Montgomery, in his Auditing—Theory and Practice, 1921 Edition, Chapter 6, speaking of how discounted notes receivable are to be handled on the books, says (p. 109):

"They represent an asset, hypothecated as it were, *against which a loan has been secured from the bank.*" (Italics ours.)

Esquerre, in his Applied Theory of Accounts, Chapter XV, pp. 159-161, discusses at length the accounting effect involved in the discounting of notes receivable, and concludes with the statement that this is what takes place:

"Notes Receivable remain unaffected in so far as the books are concerned; cash is debited with the amount received, interest and discount is debited with the amount charged by the bank, and a liability account known as 'Promissory Notes Discounted' is credited. As soon as information is obtained in regard to the payment of the notes at maturity, the liability account is debited, and notes receivable is credited with the face value of the note which has been met."

The Federal Reserve Board in its prescribed form of Balance Sheet issued for the general guidance of accountants shows:

On the debit side

"(Item 5) Notes Receivable Discounted or sold with endorsement or guaranty ..... $....."

And on the credit side

"(Item 20 (a)) Notes Receivable Discounted or sold with endorsement or guaranty (contra) ..... $....."

Modern Business—Accounting Practice and Auditing, published by Alexander Hamilton Institute, Vol. 21, Chapter 5, p. 300, cautions the accountant in regard to liability on discounted notes, and in Vol. 22, Financial and Business Statements, Chapter XIII, pp. 187-188, enters into considerable discussion of the subject arriving at the same conclusion as other authorities quoted above.

Henry Rand Hatfield's Accounting, Chapter IX, pp. 234-235, in connection with a discussion of the subject, has this to say:

> "But whether the funds are secured by endorsing the trade paper and rediscounting it, or by hypothecating it as collateral does not affect the real position of the borrower. But National banks have for long been required to show the transaction properly and instead of crediting Notes Receivable a new account, Notes and Bills Rediscounted, is credited."

Arthur Lowes Dickinson in his Accounting Practice and Procedure, Chapter VI, p. 146, deals with the subject in the same manner.

It is possible to go on with these citations throughout the long list of accounting reference works, but

surely the foregoing is sufficient to show that appellant has kept its books along the lines of sound accounting principles. By reference to "Petitioner's Exhibits 3, 4, 5 and 6 and joint Exhibit A-7," (R. 33, 36, 67, 72, 76) it will be seen from the balance sheets that appellant has followed these established rules of accounting both in keeping its books and making its tax returns.

Articles 22, 23 and 24 of Regulations 69 lay down the rule that where the books of account reflect income correctly they should not be disturbed by the examiners of appellee.

Article 23 of Regulations 69 specifically states:

> "Approved standard methods of accounting will ordinarily be regarded as clearly reflecting income."

The authorities heretofore mentioned establish beyond dispute what the *approved standard methods of accounting* are in a case where a taxpayer has discounted notes with full recourse on itself. The appellant has accordingly followed these recognized approved methods of accounting as required by the Commissioner's regulations. Certainly it should not at this time be censured or penalized for having strictly complied with these regulations.

Since the appellant has followed the approved standard methods of accounting and the regulations specifically state that such methods will ordinarily be regarded as clearly reflecting income, it is believed that this Court will recognize and sanction the principle laid down in *Ribbon Cliff Fruit Company v. Commissioner,* 12 B. T. A. 13, acquiesced in by Commissioner, C. B. VIII-1, p. 38. In its opinion in that case the Board said (Page 16):

> "There can be no question but that a taxpayer is privileged to adopt any method of accounting which it deems necessary for its business and that truly reflects its income. The statute contemplates that each taxpayer shall adopt such forms and methods of accounting as are in its judgment best suited to its purpose. Having adopted a particular method of accounting, and regularly employed that method in keeping its books, the statute requires that the taxpayer shall compute its net income, for the purposes of the tax, in accordance with that method, if income is clearly reflected thereby."

The appellant's method of accounting approved by recognized accounting authorities and which reported all of the income over a period of years and in the years when income was actually realized, correctly reported income as required by the law and regulations. The appellant's method clearly reflecting income, the Commissioner and the Board cannot substitute a method contrary to sound accounting. As stated by the Court (C. C. A. 1) in the case of *Russell v. Commissioner,* 45 Fed. (2d) 100, 101:

> "But the Commissioner's rejection of a return made by the taxpayers in accordance with its regular method of accounting is subject to review, both by the Board of Tax Appeals and by the Court. *Oesterlein Machine Company's Appeal,* 1 B. T. A. 159. An arbitrary adoption of a substitute method of computing a tax, which does not in fact 'clearly reflect the income' of the taxpayers, cannot be sustained. The Commissioner's discretion must be exercised reasonably on sound grounds."

The Board's decision approving the Commissioner's determination, namely that income was realized in 1927 when the notes were endorsed with full recourse on the taxpayer and its liability for their payment still existed, in effect sanctions a practice which is censurable not only from an accounting standpoint but from practical aspects. Taxable gain does not result from the borrowing of money. Disregarding liabilities and creating fictitious income in accounting reports has led to the unfortunate results at present confronting numerous corporate stockholders, which situations are at present in the daily news.

The only sound practice is the recognition of all actual liabilities in determining whether a corporation has in fact realized income. This Court should so hold and reverse the decision of the Board of Tax Appeals which in effect would permit and force the creation of imaginary income before it is realized.

Taxable Income and Profit From the Transaction Could not be Determined in 1927.

Eliminating from this case any controversy as to whether notes were sold or money loaned upon them or whether the Board's decision is in conflict with sound accounting practice, one factor nevertheless remains and that is that the Alworth-Washburn Company did not and could not realize in 1927 the income or profit reflected in the installment notes.

The realization of income or losses is dependent upon a completed and closed transaction and not until a taxpayer definitely knows that its right to income has been definitely fixed, is such income taxable to it.

As stated by the Court (C. C. A. 6) in the recent case of *Commissioner of Internal Revenue v. R. J. Darnell, Inc.*, 60 Fed. (2d) 82, 84:

> "Income taxes are properly assessed upon the basis of annual returns (*Burnet v. Sanford & Brooks Co.*, 282 U. S. 359); but 'generally speaking the income tax law is concerned only with realized losses, as with realized gains' (*Lucas v. American Code Co.*, 280 U. S. 445, 449); and if income has neither actually been received during the taxable year, nor the right to its receipt been definitely fixed during that year, as to both the existence of an obligation on the part of the payor and the amount to be paid, such income is properly to be allocated to that year in which it was in fact received or in which the right to receipt became fixed and liquidated. This is the true and full effect of the decisions in *Lucas v. North Texas Company*, 281 U. S. 11; *Burnet v. Sanford & Brooks Co.*, 282 U. S. 359; and *North American Oil Consolidated v. Burnet*, 286 U. S. 417."

It is difficult to imagine how a *realized gain* resulted from the discount of the notes in question as long as the appellant's liability to make good the payments remained. Not until the year 1928 and subsequent years was the income in the notes actually received proratably, by the appellant and the maker's indebtedness on the notes liquidated. Until that time the advances received from the bank were encumbered with the definite liability of repayment by the appellant. Not until the years subsequent to 1927 could anyone contend that the transaction in question was closed and completed.

If the discount of the notes with the First National Bank of Minneapolis completed the transaction, as the

Board has held, it is reasonable to assume that the corporation would have been dissolved and further expense in connection with its maintenance avoided.

But Sections 8015 and 8019 of the General Laws of Minnesota, 1923 (in effect in 1927), prohibited the voluntary dissolution of a corporation as long as there are any assets and liabilities to be disposed of. Had appellant, upon the discounting of the notes in 1927, petitioned the courts for dissolution, it is clear such petition would have been rejected until such time as the company's liability as endorser had been discharged. The discounting bank would not have permitted the appellant to free itself from its liability to the bank through the process of dissolution.

Again the decision of the Board holding that net taxable income or profit reflected in the notes was determined and realized in 1927 and the transaction completed in that year, distorts income for the year 1927 in that it ignores certain expenses which are part and parcel of the transaction. There were necessary expenses incident to the maintenance of appellant's corporate status after 1927. The appellant's only assets after that time were these notes receivable and since these assets and the liability in connection therewith constituted the only reason for the maintenance of the corporate existence, it is evident that such expenses are directly attributable to and deductible from any gross profit reflected in the notes. Such expenses incurred by the appellant in the years subsequent to 1928 were as follows: For 1928, $2,874.00 (R. 63), for 1929 $1,003.35 (R. 68), for 1930 $1,335.54 (R. 72) and for 1931 about $1,500.00 (R. 23), or a total of $6,712.89.

Accordingly, the *net taxable income* or profit reflected in the notes could not accurately be determined

as early as the year 1927. The effect of the Board's decision in this case is to deprive appellant of deductions in the nature of ordinary and necessary expenses to which it is clearly entitled. The continuing expenses of corporate existence cannot be disassociated from the income contained in the notes and to hold that *net income* resulted from the discount of the notes in 1927, disregards a vital element, namely, expenses of the transaction.

Finally it may be contended that while the appellant was liable for the payment of the Brooks-Scanlon notes, the record shows the notes were in fact all paid by the Brooks-Scanlon Lumber Company and therefore the Board was correct in holding the transaction completed in 1927.

Such contention, however, is completely answered when it is remembered that income taxes are imposed on an annual basis and income must be determined by the facts as they existed in 1927—not in 1931. Appellant's liability existed one hundred per cent at the time of the discount in 1927. The transaction could not be considered closed and completed in 1927 by a retrospective view of the situation in 1931.

CONCLUSION.

The decision of the Board of Tax Appeals is contrary to the rule of law relating to unqualified endorsements, unsupported by any substantial evidence and contrary to all of the material evidence, contrary to all sound accounting methods and in conflict with the established principles and rules of income taxation.

It is, therefore, prayed that this Court reverse the decision of the United States Board of Tax Appeals with directions to the Board to find that no income was realized in 1927 by appellant from the discount of the notes of the Brooks-Scanlon Lumber Company; and with directions to the Board to redetermine appellant's taxes accordingly.

Respectfully submitted,

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COURT OF APPEALS
DISTRICT OF COLUMBIA
FILED

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No. 585

In the Court of Appeals of the District of Columbia

OCTOBER TERM, 1932

ALWORTH-WASHBURN COMPANY, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ON PETITION FOR REVIEW OF DECISION OF THE UNITED STATES BOARD OF TAX APPEALS

BRIEF FOR THE RESPONDENT

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In the Court of Appeals of the District of Columbia

OCTOBER TERM, 1932

No. 5858

ALWORTH-WASHBURN COMPANY, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, respondent

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ON PETITION FOR REVIEW OF DECISION OF THE UNITED STATES BOARD OF TAX APPEALS

BRIEF FOR THE RESPONDENT

PREVIOUS OPINION

The only previous opinion in the present case is that of the United States Board of Tax Appeals (R. 8–10), which is reported in 25 B.T.A. 140.

JURISDICTION

This appeal involves income taxes for the year 1927 in the amount of $19,005.60 and is taken from a decision (order of redetermination) of the United States Board of Tax Appeals entered January 14, 1932 (R. 10–11). The case is brought to this

Court, under stipulation by the parties (R. 11), by petition for review filed July 13, 1932 (R. 12–16), pursuant to the Revenue Act of 1926, c. 27, 44 Stat. 9, 109 110 Sections 1001, 1002, and 1003 (U.S.C., Supp. VI, Title 26, Secs. 641–642).

QUESTION PRESENTED

Where the petitioner in 1927 endorsed in blank and transferred to a bank the notes of the purchaser of property sold by it in 1926 upon the installment plan, is the cash received from the bank in excess of that amount of the notes representing unrecovered cost (or other basis) of the property taxable income for 1927, when received, or is such excess taxable income only in proportionate amounts for the respective years in which the notes are paid?

STATUTES AND REGULATIONS INVOLVED

The applicable provisions of the statutes and regulations involved are set forth in the appendix, *infra,* pp. 25–28.

STATEMENT

The petitioner, a Minnesota corporation with its principal office at Duluth, Minnesota (R. 3, 8), in 1926 sold to the Brooks-Scanlon Lumber Company, a Minnesota corporation, 12,440 acres, more or less, of timber land (R. 8, 17, 26). The land had been acquired by petitioner for resale rather than for operation and at the time of sale constituted the remainder of its assets (R. 8, 18, 22). The sale

price as stipulated in the contract of sale was $590,900, payable $100,000 cash at the time of sale and the balance in five equal annual installments of $98,180 each on May 1st of each year following (R. 8, 26–27). Thereafter the sale price was adjusted to $588,838.02, the 1926 payments to $121,-118.02 and the May 1, 1927, payment to $75,000, the last four installments remaining in the same amounts as provided for in the contract (R. 8–9, 17, 54, 76, 79). The deferred payments, or installments, of the sale price were evidenced by five series of promissory notes made by the purchaser, Brooks-Scanlon Company, payable to the order of the petitioner, with interest at 5 percent per year payable annually (R. 8, 27, 47).[1] The contract provided that upon payment of the full sale price the petitioner should execute to the Brooks-Scanlon Company a warranty deed covering the property sold (R. 28).

In making its tax return for 1926 the petitioner elected to report the profit on the sale upon the installment basis, including in that return as gross receipts the payments of $121,118.02 received in 1926 (R. 9, 49, 54). The installment of $75,000 due on May 1, 1927, was collected by the petitioner and reported on its 1927 tax return as gross receipts during that year from the sale (R. 9, 76, 79).

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[1] The figure of 6 percent appearing in the opinion of the Board (R. 8) as the rate of interest payable on the deferred installments is obviously a typographical error or a mistake.

On December 6, 1927, the petitioner endorsed in blank the notes for the remainder of the sale price, consisting of four series of notes in the principal amount of $98,180 for each series or an aggregate of $392,720, and discounted or sold the same to the First National Bank of Minneapolis, receiving therefor the total sum of $403,882.93 in cash (R. 9, 19, 38–39). On December 21, 1927, the petitioner delivered to the bank its warranty deed conveying the land to the Brooks-Scanlon Company, to be held in escrow for delivery to the Brooks-Scanlon Company when the remainder of the notes representing the unpaid balance of the sale price were paid or taken up (R. 20, 39). All the proceeds received from the disposition of the notes, except a small amount retained to meet tax obligations and other expenses, were immediately distributed to the stockholders of the petitioner and entered on the books as advances (R. 9, 24, 39). All the notes as they became due were paid by the Brooks-Scanlon Company, maker (R. 9, 24, 81).

On its 1927 tax return the petitioner did not report any part of the proceeds received upon the disposition of the notes to the First National Bank, but continued in subsequent years to report the profit from the sale of the land upon the installment basis, including in its return for each year the amount of the notes as paid to the bank (R. 9, 63–79). Subsequent to 1927 the only activities of the petitioner have been to inquire from time to time about the payment of the notes by the maker and

to prepare federal and state tax returns, and during such years the average operating expense of the petitioner totaled about $1,500 a year, consisting of license fees to certain states and audit expenses (R. 23–24). The respondent found that the profit realized by the petitioner upon the disposition of the installment notes to the bank on December 6, 1927, was taxable income for 1927 and accordingly determined a deficiency in tax for that year in the amount of $19,005.60 (R. 6). The Board of Tax Appeals sustained the determination of the respondent (R. 10–11).

SUMMARY OF ARGUMENT

The statute provides that the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the cost or other basis of the same. "Gross income" is defined to include gains or profits derived from dealings in property and from any source whatever. All gains or profits and income must be included in gross income for the taxable year in which received. The statute, however, authorizes the return of profit from the sale of real property upon the installment basis, where the initial payments do not exceed one fourth of the purchase price.

In 1926 the petitioner sold real property and then received cash payments less than one fourth of the purchase price, the balance being payable in five annual installments (the last four in equal

amounts), for which five series of interest-bearing notes were taken. In May 1927 petitioner collected the first installment. In December 1927 petitioner sold the remaining notes, endorsed in blank, to the First National Bank of Minneapolis for cash. The cash received for the notes exceeded the cost thereof (the unextinguished cost or other basis of the land).

The endorsement of the notes to the Bank for cash was not a loan, but was a sale of the notes by the petitioner. It would be a most unnatural thing to call such a transaction a loan. By the endorsement and transfer of the notes the petitioner finally disposed of all its interest therein and in the land for which they were taken. The liability of the petitioner upon the notes as endorser was only secondary and contingent and could not suspend the finality of the sale or defer the receipt of the profit as taxable income beyond the year in which actually received. Had the petitioner been forced to pay any part of the notes because of the default of the maker, it would have sustained a loss in the year of such payment. The profit derived from the sale, however, is taxable income for the year it was received and the taxation thereof may not be postponed because of the possibility that a loss might have been sustained in a later year. It will be noted, moreover, that petitioner sustained no loss by reason of its contingent liability, for the notes were promptly paid by the maker at maturity.

The profit derived by petitioner upon the endorsement and transfer of the notes to the Bank for cash in December 1927 is taxable income for that year and the Board of Tax Appeals correctly so held.

ARGUMENT

Upon the endorsement in blank and transfer of the installment notes by the petitioner to the bank on December 6, 1927, for cash the petitioner realized income taxable in full in 1927

The only question in this case is whether the petitioner derived or realized taxable income in 1927, when on Decemebr 6th of that year it endorsed in blank the notes of the Brooks-Scanlon Company, which represented the balance of the sale price of the timberland sold in 1926, and transferred the same to the First National Bank for cash. The petitioner contends that the notes were not sold to the Bank, but by virtue of its endorsement the cash received upon the notes was a loan from the Bank to it, that since the sale of the land in 1926 was an installment sale the profit may be apportioned to the several installments and is taxable income to it, in proportionate amounts, only in the respective years in which the notes were paid by the maker. The respondent contends that, although the land was sold upon the installment plan and the petitioner was entitled to report the profit for 1926 upon the installment basis, the transfer of the notes by endorsement to the Bank for cash in 1927 was a

sale thereof and the entire profit thereby derived or realized was taxable income for 1927.

The statute provides that the gain derived from the sale or other disposition of property shall be the excess of the amount realized (i.e., any money received plus the fair market value of other property received) over the cost of the property or its March 1, 1913, value, if acquired prior to that date, and such value exceeds cost. Sections 202 (a) (c) and 204 (a) (b). Gains, profits, and income derived from sales or dealings in property, growing out of the ownership or use of or interest therein, and income derived from any source whatever, are included in "gross income", as defined, and the amount of all such gains, profits, and income must be included in the gross income for the taxable year in which received unless properly to be accounted for in some other year upon an authorized basis of accounting. Section 213 (a). The net income, which is the subject of the tax and is defined as gross income less specifically authorized deductions (Sec. 212 (a)), must be computed upon the basis of the taxpayer's annual accounting period and in accordance with its regular method of accounting if true net income is thereby clearly reflected. Section 212 (b). It is further provided, however, that in the case of a sale of real property, if the payments in cash or other property received during the taxable year (initial payments) do not exceed one fourth of the purchase price, the taxpayer may report the profit

therefrom upon the installment basis. Section 212 (d).

The petitioner sold its timberland in 1926 to the Brooks-Scanlon Company for the total price of $588,838.02, of which $121,118.02 was paid during the year and $75,000 was paid on May 1, 1927. The balance of the purchase price was payable in four equal annual installments of $98,180 each, for which the purchaser executed four series of promissory notes payable to the order of the petitioner. On December 6, 1927, the notes aggregating $392,720 in principal and bearing interest at 5 percent per year, were endorsed in blank by the petitioner to the Bank for $403,882.97 cash, the petitioner depositing in escrow with the Bank a warranty deed to the land to be delivered to the purchaser upon payment of the notes.

From these facts it is obvious that the sale in 1926 was an installment sale of real property, for the initial payments received during the year were less than one fourth of the total purchase price, and under the statute the petitioner was entitled, and permitted, to report the profit for that year upon the installment basis. Similarly, the May 1, 1927, installment of $75,000 was returnable upon the installment basis and had the petitioner retained the remaining installment notes there would have been no further income from the sale of the land returnable and taxable for 1927.

The petitioner, however, after 1927 did not continue to hold the notes for the remaining install-

ments due on the purchase price of the land. On December 6, 1927, it endorsed the notes in blank and sold them to the Bank for cash. Those notes, taken by the petitioner as part consideration for the land, stood in the place of the land for which they were received and represented property in the hands of the petitioner to the same extent as the land itself. See *Nichols* v. *Fearson,* 7 Pet. 103, 108–109, where it was said:

> But he who sells his lands or stock, and takes a note in payment, holds in his hands the representative of property; an entity to which the improvements of society have attached nearly all the rights and characteristics, in equity, at least, which were the acknowledged attributes of the property for which it was received.

By the endorsement and transfer of the notes to the Bank the petitioner sold or otherwise disposed of property and received cash therefor. The amount of cash received in excess of the cost or other basis of the notes was a gain or profit and income derived or realized by the petitioner in 1927 and under the plain language of the statute must be reported and taxed as income for that year.[2]

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[2] The *amount* of gain realized from the disposition of the notes, as determined by the respondent, is conceded by the petitioner, we understand (R. 9). Generally speaking, such gain is the amount of cash received in excess of the proportion of the notes representing the cost or other basis of the land not already returned to the petitioner through the installments previously collected.

It is wholly immaterial that the sale of the land in 1926 was an installment sale and the profit therefrom for that year was properly returnable upon the installment basis. The disposition of the remaining installment notes in 1927 was another and separate transaction and, although growing out of the original sale of 1926, is not affected by the nature of the earlier sale. Upon the endorsement of the notes to the Bank and the receipt of cash therefor by the petitioner it received payment in full for its property and thereafter owned no interest therein. Upon receipt of the cash from the Bank for the notes the petitioner realized income from the sale or other disposition of property which is taxable for 1927, the year in which received.

In *Elmer* v. *Commissioner* (C.C.A. 2d), decided June 5, 1933, not yet reported, but may be found in 333 C.C.H., 8933, the taxpayer sold automobiles upon the installment plan. A small down payment in cash was made and the balance of the purchase price, payable over a period of about 18 months, was evidenced by a series of interest-bearing notes secured by a conditional sale contract reserving title in the seller. The taxpayer endorsed the notes to a finance company, assigning his interest in the contracts, and received therefor the face amount of notes, representing the unpaid purchase price, less certain charges, in cash. The taxpayer sought to report the profit on the sales upon the installment basis, contending that the amount received from

the finance company was a loan and the profit represented by the notes was taxable as income in proportionate amounts only in the year in which the notes were paid by the purchaser. The court holding that the endorsement and transfer of the notes to the finance company for cash was a sale, not a loan, and that the profit was taxable income in its entirety for the year in which the amount was received, said (pp. 8933–8934):

> Such transactions are somewhat ambiguous and admit of definition as loans or sales on slight differences. If a merchant discounts his customer's note at a bank, endorsing it, but getting immediate credit for its discount value, it would be a most unnatural thing to consider it a loan from the bank. He remains liable if the customer defaults, but the collection is in the bank's hands, and the transaction is closed in the absence of default. If, on the other hand, a merchant pledges his accounts to a "finance" company and collects them himself, paying the loan out of his collections, it is clearly a loan, and has always been so considered. * * * These transactions were different; the finance companies collected the notes themselves, and, as we have said, if the customer did not default, the dealer had no more to do than if he had discounted his note with a bank. Nor was there any equity in the assigned accounts for which the companies were responsible to the dealer; the full amount was paid, less a somewhat nebulous

"interest" charge, which gave the companies a profit of more than the interest on the customer's note. * * * In any event, the dealer's liability was only to pay what remained of the customer's debt; he never became liable for the original advance he had received. * * * It is possible, as we have suggested, to construe these transactions in either way. We incline to consider them as more nearly analogous to discounts, because they were closed transactions unless the customer defaulted, the dealer having nothing to do with collection; because there was no equity to be remitted; because, though the dealer was to enforce the collateral, he may have done so as agent for the company, which remained entitled to the proceeds; and because he was never liable for the advances as such.

The instant case is substantially on all fours with the *Elmer case.* The fact that there the notes were endorsed and discounted with a finance company in the same year of the sale of the automobiles, while here the notes were endorsed and discounted with a bank in the year following the sale of the land, is not a material distinction. In this case, as in the *Elmer case,* the installment notes were endorsed to a third party and cash received therefor, the endorser was liable, conditionally, to the endorsee or holder of the notes in the event the maker defaulted but not otherwise. Here, as in the *Elmer case,* the notes were sold and the profit thereby realized was

taxable income for the year in which the cash for the notes was received.

In *Duram Building Corp'n* v. *Commissioner* (C.C.A. 2d), decided July 5, 1933, not yet reported, but may be found in 333 C.C.H., 9104, it was held that the transfer by the taxpayer of installment notes of the purchaser of property, sold by the taxpayer on the installment plan, to a third party for the cancellation of a debt owing by the taxpayer, was a sale of the notes for cash or its equivalent and the gain thereby realized was taxable income for the year in which the notes were transferred. In that case the notes were disposed of during the year the original property was sold and the Board of Tax Appeals had held that the amount received therefor should be included in the "initial payments", which on that basis exceeded one fourth of the purchase price and precluded the use of the installment basis for reporting income. The court rejected the view of the Board that "initial payments" include amounts received by the seller of property on the installment plan from third persons for installment obligations of the purchaser, but held, as stated above, that the profit realized upon the disposition of such installment obligations was income for the year in which the amount therefor is received. In this connection the court said (p. 9106):

> To the extent that the purchase money notes and mortgages paid this debt the corpora-

> tion is in the same position as if it had sold a portion of them for cash and used the cash to pay its debt. See *Batcheller* v. *Commissioner,* 19 B.T.A. 1050. On this disposal of the mortgage notes at face value in the amount of the debt, it realized a profit which it must return for taxation.

The decisions of the Board of Tax Appeals are to the same effect. *Shubin et al.* v. *Commissioner,* 25 B.T.A. 792; *W. F. Gillies* v. *Commissioner,* 20 B.T.A. 570; *E. E. Chapman* v. *Commissioner,* 19 B.T.A. 878; *W. H. Batcheller* v. *Commissioner,* 19 B.T.A. 1050; *Packard Cleveland Motor Co.* v. *Commissioner,* 14 B.T.A. 118; *Grace T. Mytinger* v. *Commissioner,* 4 B.T.A. 896. While the decisions of the Board in most cases involving the question have gone further and required that the amount received from third persons for installment obligations of the purchaser be included in "initial payments", when received during the year of sale of the original property, those cases are in entire accord with the *Elmer* and *Duram* cases in holding that the taxpayer realizes gain or profit upon the disposition of installment notes or obligations which is taxable income for the year in which the notes or obligations are disposed of.

That the sale or other disposition of installment notes received in payment of property sold on the installment plan, as in the instant case, is a separate transaction from the original sale in connection with which the notes were received and is one giv-

ing rise to a taxable gain in the year of their disposition, is expressly recognized by Section 44 (d) of the Revenue Acts of 1928 c. 852, 45 Stat. 791, and 1932 c. 209, 47 Stat. 169. Although those statutes do not govern the transaction here in question, which took place in 1927 and is controlled by the Revenue Act of 1926, it is believed that they express the rule equally applicable under the general provisions of the earlier act. See *Duram Building Corp'n* v. *Commissioner, supra,* where it was said (p. 9105):

> Moreover, when the vendor disposes of the purchaser's notes he enters into a separate transaction with a third party which may itself result in profit or loss. See *Alworth-Washburn Co.* v. *Commissioner,* 25 B.T.A. 140. This is expressly recognized by section 44d of the Revenue Act of 1928. 26 U.S.C.A., sec. 2044. That statute, of course, is not controlling as to the petitioner's transactions in 1926; but we view it as merely an express recognition of what was equally true under the 1926 Act by reason of the general provisions (section 202–204) with respect to the sale of property by a taxpayer. Compare *Meagher* v. *Com'r,* 20 B.T.A. 68, 72; *Va. Beach Corp.* v. *Com'r,* 23 B.T.A. 1170, 1175. Therefore, as we interpret section 212(d), the privilege of reporting upon the instalment basis depends upon the transactions between the vendor and purchaser of the land during the taxable period; it is not made conditional upon what disposition the

> vendor may make of the purchaser's evidences of indebtedness by transactions with third parties during the taxable period in which the land was sold. Such transactions are separate and independent and will themselves be the basis for a return of profit or loss.

It will be noted that the court there cites the Board's decision in the instant case with apparent approval.

The petitioner argues that the transfer of the notes to the Bank was not a sale thereof, but that the amount received from the Bank was a loan advanced upon its endorsement of the notes. The argument is predicated upon the proposition that the endorsement itself imports a loan, as does the statement that the notes were discounted by the Bank, and in support thereof the petitioner cites a number of cases involving the question whether the rate at which a note endorsed by the payee was discounted was prohibited by the usury statutes. Although the opinions of the courts in those cases contain general statements which lend some support to petitioner's contention, it must be borne in mind that the courts had under consideration whether the particular transactions were in fact loans and in contravention of the statutes against usury.

We do not believe that the decisions can be taken to hold that every endorsement and discount of a note is *per se* a loan, for neither the term *endorse-*

ment nor the term *discounted* necessarily implies a loan from the endorsee to the endorser. The endorsement of a note is a separate contract or undertaking by which the owner of the debt evidenced by the note transfers title thereto. It is but a conditional or provisional contract in the nature of a guaranty and may be no more than a sale of the note evidencing the debt, which is property. *Nichols* v. *Fearson, supra.* The contract of the endorser is that he will pay the note to the holder *if not paid by the maker* at maturity. *Franklin* v. *Browning,* 117 Fed. 226, 227 (C.C.A. 8th). Likewise the term *discounted* is equally applicable to a *purchase* of a note at a discount, i.e., for a sum less than its face, as to a loan the interest upon which is taken in advance. *Danforth* v. *National State Bank of Elizabeth,* 48 Fed. 271, 274 (C.C.A. 3d). Without more, it cannot be said that in all cases the endorsement and discount of a note necessarily is a loan from the endorsee to the endorser. A sale is the transfer of property for a price in money, whereas a loan of money is a contract whereby one party receives a sum of money from another and *agrees to repay absolutely such sum* together with an additional amount for its use. *In re Grand Union Co.,* 219 Fed. 353, 356 (C.C.A. 2d). A brief reference to the record in this case will demonstrate that the cash paid to the petitioner for the notes was not a loan but the transaction was essentially a sale.

The petitioner endorsed the notes in blank and thereby transferred absolute title thereto to the

Bank. That the parties themselves so understood the transaction is evidenced by the testimony of petitioner's witness that the notes belonged to the Bank and petitioner was on the notes only as endorser (R. 21). Although the witness also said that petitioner could have made arrangements to take the notes if agreeable to the Bank, it is apparent that such testimony means nothing more than that the petitioner might have been able to repurchase the notes at a price agreeable to the Bank (R. 21). The witness also said that bills discounted means the same thing in banking parlance as loans made (R. 19), and that so far as the bank was concerned the transaction would be identical whether the petitioner gave its own note with the other notes as collateral or, as was actually done, endorsed the purchaser's notes to the bank (R. 20). Such testimony can mean only that the bank would in the latter event demand payment of the petitioner *if the maker defaulted,* for it is obvious that the two undertakings are not identical. On its own note the petitioner would be primarily and absolutely liable to repay the amount received at maturity, whereas on its endorsement of another's notes the petitioner would be only secondarily or conditionally liable to pay the bank *if the maker did not.*

The witness himself recognized this distinction when he said that "if the notes had not been paid the bank would have looked for payment to the" petitioner (R. 20). The witness further pointed out that if a loan had been made to petitioner, in-

stead of discounting the notes of the purchaser endorsed by petitioner, the bank would have had a note signed by the petitioner, but in this instance they had no note of the petitioner—only Brooks-Scanlon notes endorsed (R. 21). It was also testified that the amount of the notes would not have been applied to petitioner's line of credit, as in the case of a loan, because it was the obligation of another person (R. 22). Finally, the resolution of the directors of the petitioner authorizing, ratifying and confirming the disposition of the notes in question shows that the petitioner knew it was making a sale of the notes and was not obtaining a loan (R. 37–40). It is also significant that although the principal amount of the notes aggregated only $392,720, the petitioner received from the Bank $403,882.93 therefor, which seems to negative a loan on discount and is more consistent with a sale of the interest-bearing notes for an agreed price. Moreover, all of the proceeds, except a small amount retained for certain tax obligations (was immediately distributed to the stockholders.

The fact that the petitioner set up on its books the distributions to stockholders as advances and made other entries on its records of the notes as a liability offset by the same amount as receivables, cannot be considered determinative of the character of the transaction disposing of the notes. The books are at best merely evidential and are neither indispensable nor conclusive—the actual facts must

control. *Doyle* v. *Mitchell Bros. Co.,* 247 U.S. 179, 187. Nor is it at all material that the petitioner continued its corporate existence after the notes were sold and incurred minor expenses without deriving income against which to offset such expenses, for it is not uncommon for a taxpayer to incur expenses or sustain losses and derive no benefit therefrom by way of tax reduction, because of the absence of income from which to deduct the same. The facts in this case show that the receipt of cash by petitioner for the notes endorsed and transferred to the Bank in 1927 was not a loan, but was a sale of the notes by the petitioner to the Bank. As said by the court in *Elmer* v. *Commissioner, supra*—

> If a merchant discounts his customer's note at a bank, endorsing it, but getting immediate credit for its discount value, it would be a most unnatural thing to consider it a loan from the bank. He remains liable if the customer defaults, but the collection is in the bank's hands, and the transaction is closed in the absence of a default.

The position of the petitioner is nothing more than an attempt to postpone the taxation of the gain derived in 1927 from the disposition of the notes upon the ground that because of its endorsement it was liable for the repayment of the amount of the notes if the maker, Brooks-Scanlon Company, defaulted. The petitioner's liability upon its endorsement, however, was only contingent or con-

ditional, as heretofore pointed out. Until the maker defaulted petitioner could incur no loss. Notwithstanding such liability, the fact remains that the petitioner sold and transferred the notes to the Bank. Thereby the petitioner disposed of all its interest in the property, the notes as well as the land for which they were given, and received therefor payment in full. The transaction was then closed and to the extent that the cash received represented profit the petitioner derived taxable income. The finality of the transaction was not suspended and the receipt of taxable income therefrom was not deferred or postponed by the possibility that the petitioner at some future date might be held accountable upon its contingent liability. The petitioner might have sustained a loss if the Brooks-Scanlon Company defaulted in payment and it had to pay the notes, but the gain was derived and taxable income was received by the petitioner in 1927 when it disposed of the notes and received payment.

It must be regarded as settled that gain or income is taxable in the year in which received, although the right thereto may be disputed and even though there exists some liability by reason of which a loss may be sustained or there may have been or may be incurred or sustained expenses or losses in some other year in connection with the earning of such income. See *North American Oil Consolidated* v. *Burnet,* 286 U.S. 417; *Burnet* v. *Sanford &*

Brooks Co., 282 U.S. 359; *Fawsett* v. *Commissioner,* 63 F. (2d) 445 (C.C.A. 7th), petition for certiorari now pending; *Clemmons* v. *Commissioner,* 54 F. (2d) 209 (C.C.A. 5th); *Ford* v. *Commissioner,* 51 F. (2d) 206 (C.C.A. 6th), certiorari denied, 284 U.S. 666; *Board* v. *Commissioner,* 51 F. (2d) 73 (C.C.A. 6th), certiorari denied, 284 U.S. 658; *Commissioner* v. *Moir,* 45 F. (2d) 356 (C.C.A. 7th).

These cases establish the principle that a transaction otherwise closed is not uncompleted and that the receipt of income is not postponed or deferred for purposes of taxation beyond the year in which it is actually received, merely because there exists some potential liability which may give rise to a loss or because some loss or expense incident thereto may be or may have been sustained or incurred in some other year.

The instant case, we submit, clearly is controlled by this principle. In December 1927 the petitioner finally disposed of the notes, and thereby all its interest in the land, and received in payment therefor cash in an amount exceeding the cost of the notes (the unextinguished remainder of the cost or other basis of the land). The excess amount so received manifestly is income under the statute which is taxable in 1927, the year in which received notwithstanding a loss might be sustained at a later date by reason of its liability as endorser. Had it been forced to pay the Bank any amount on its endorsement, by reason of the default of Brooks-Scanlon

Company, the resulting loss, if any, would be deductible in the year such payment was made, but until it paid the notes, in whole or in part, it sustained no loss. See *North American Oil Consolidated* v. *Burnet, supra; Burnet* v. *Huff,* 288 U.S. 156; *Eckert* v. *Burnet,* 283 U.S. 140. It should be noted, however, that the petitioner sustained no loss on the notes by reason of its liability as endorser, for it was not required at any time to pay any amount thereon. The notes were promptly paid at maturity by the maker, Brooks-Scanlon Company.

CONCLUSION

The decision of the Board of Tax Appeals is correct and should be affirmed.

Respectfully submitted.

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APPENDIX

Statutes and Regulations Involved

REVENUE ACT OF 1926, C. 27, 44 STAT. 9

Sec. 202. (a) Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in subdivision (a) or (b) of section 204, and the loss shall be the excess of such basis over the amount realized.

* * * * *

(c) The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received. * * * U.S.C. App., Title 26, Sec. 933.)

Sec. 204. (a) The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; * * *

* * * * *

(b) The basis for determining the gain or loss from the sale or other disposition of property acquired before March 1, 1913, shall be (A) the cost of such property (or, in the case of such property as is described in paragraph (1), (4), or (5), of subdivision (a), the basis as therein provided), or (B) the fair market value of such property as of March 1, 1913, whichever is greater. In determining the fair market value of stock in a corporation

as of March 1, 1913, due regard shall be given to the fair market value of the assets of the corporation as of that date. * * * (U.S.C.App., Title 26, Sec. 935.)

SEC. 212. (b) The net income shall be computed upon the basis of taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. * * *

* * * * *

(d) Under regulations prescribed by the Commissioner with the approval of the Secretary, a person who regularly sells or otherwise disposes of personal property on the installment plan may return as income therefrom in any taxable year that proportion of the installment payments actually received in that year which the total profit realized or to be realized when the payment is completed, bears to the total contract price. In the case (1) of a casual sale or other casual disposition of personal property for a price exceeding $1,000, or (2) of a sale or other disposition of real property, if in either case the initial payments do not exceed one fourth of the purchase price, the income may, under regulations prescribed by the Commissioner, with the approval of the Secretary, be returned on the basis and in the manner above prescribed in this subdivision. As used in this subdivision the term "initial payments" means the payments received in

cash or property other than evidences of indebtedness of the purchaser during the taxable period in which the sale or other disposition is made (U.S.C. App., Title 26, Sec. 953).

SEC. 213. For the purposes of this title, except as otherwise provided in section 233—

(a) The term "gross income" includes gains, profits, and income derived from * * * dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; * * * or gains or profits and income derived from any source whatever. The amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period. * * * (U.S.C.App., Title 26, Sec. 954.)

SEC. 232. In the case of a corporation subject to the tax imposed by section 230 the term "net income" means the gross income as defined in section 233 less the deductions allowed by sections 234 and 206, and the net income shall be computed on the same basis as is provided in subdivisions (b) and (d) of section 212 or in section 226. * * * (U.S.C.App., Title 26, Sec. 984.)

SEC. 233. (a) In the case of a corporation subject to the tax imposed by section 230 the term "gross income" means the gross income as defined in sections 213 and 217, except that mutual marine insurance companies shall include in gross income the gross premiums collected and received by them less amounts paid for reinsurance * * * (U.S.C. App., Title 26, Sec. 985).

ART. 31. *What included in gross income.*—Gross income includes in general * * * profits from sales of and dealings in property, * * * and gains, profits, and income derived from any source whatever, unless exempt from tax by law. * * *

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